Financial & Compliance Audit Manual

Office of the Comptroller and Auditor General of Bangladesh

Preface

The Supreme Audit Institution (SAI) of Bangladesh always keeps itself abreast of what is happening in the contemporary audit world. The global platform of the Auditors General (i.e., INTOSAI) issued International Standards of Supreme Audit Institutions, commonly known as ISSAIs in 2010 for the guidance of government auditors across member nations. If these professional standards are followed in the SAI of Bangladesh, it will enhance the quality and efficiency of government auditors and help them in playing their entrusted role. The present Manual is based on the ISSAIs.

This Financial and Compliance Audit Manual is a very important deliverable under the present development initiative, i.e., Strengthening the Public Expenditure Management Programme (SPEMP-B). International and national consultants and the members of the evaluation team deserve special appreciation for contributing to this valuable product. Meanwhile, pilot audits have been carried out in line with the Manual. From now on financial and compliance audit will be conducted as per the Manual and other audit standards and codes.

This Manual is relatively more comprehensive in scope than other existing Manuals in the sense that it contains two major types of audit, namely, financial audit and compliance audit. The Manual derives its authority from articles 128 and 132 of the Constitution of the People's Republic of Bangladesh and the Comptroller and Auditor General (Additional Functions) Act, 1974 and subsequent amendments thereof.

This Manual is a living document. It will be updated periodically or as and when necessary. Any suggestion to improve it will be most welcome. However, while applying the Manual if any error or omission is noticed, it may please be brought to the notice of the Office of the Comptroller and Auditor General of Bangladesh immediately for due rectification.

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Comptroller and Auditor General of Bangladesh

Dated: Dhaka, May 2016

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Chapter 1 Introduction

1.0 Introduction

1.1. The International Organisation of Supreme Audit Institutions (INTOSAI) has issued "Fundamental Principles of Financial Auditing" as International Standards of Supreme Audit Institutions (ISSAI) 200, and Financial Audit Guidelines (ISSAI 1000-1810) provide guidance for conducting financial audits of public sector entities and include the International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB).

1.2. Practice Notes (PN), which are included in the INTOSAI Financial Audit Guidelines, provide relevant guidance on applying each ISA in financial audits of public sector entities in addition to that provided in the corresponding ISA.

1.3. INTOSAI has also issued Fundamental Principles in Compliance Auditing (ISSAI 400) to give specific guidance on audit and reporting responsibilities relating to compliance with authorities. This is supported by General Auditing Guidelines on Compliance Audit (ISSAI 4000, 4100 and 4200). ISSAI 4100 provides guidance for compliance audits performed separately from the audit of financial statements whereas ISSAI 4200 provides compliance audit guidelines related to audit of financial statement. They build upon INTOSAI's Fundamental Auditing Principles and have been designed to assist public sector auditors having responsibilities related to compliance with authorities. ISSAI 4100 and 4200 supplement, should be read together with the Financial Audit Guidelines (ISSAI 1000-2999), when having such broader responsibilities.

1.4. This OCAG Financial and Compliance Audit Manual draws on the guidance in ISSAI 1000-2999 and 4000-4200 and interprets the way that this guidance is to be implemented by the Office of the Comptroller and Auditor General in conducting both financial and compliance audits in public sector entities of Bangladesh.

1.5. This Manual has been developed to provide OCAG auditors with a set of modern financial and compliance auditing standards, concepts, techniques and quality assurance arrangements that are consistent with the international standards as detailed above.

1.6. The purpose of this Audit Manual is to promote consistency and efficiency in the conduct of audits, and to enhance the quality of audit work.

1.7. OCAG auditors are expected to exercise professional judgement in the application of the principles detailed in this Manual.

1.8. This Manual is equally applicable to compliance and financial audits. Some of the text is specifically applicable only to financial audits (e.g. paragraphs 4.69 to 4.82).

1.9. All OCAG auditors are required to familiarize themselves with the contents of the Manual to use it as a reference for conducting audits.

1.10. To promote consistency in its approach to audit and in its operations, OCAG must have an up to date Audit Manual giving guidance on policies and procedures for functions and processes. This manual has to be revised or updated whenever there are changes in the audit objectives, standards and techniques and any other laws, policies and applicable directives given by the Government of Bangladesh.

1.11. The SAI Bangladesh published audit manuals under previous reform initiative known as Reforms in Government Audit (RIGA) as per the then available standards. These manuals continue to be used side by side with this currently available Audit Manual prepared based on ISSAIs.

1.12. Audit staff who identify the need for revisions or have suggestions for improvement are encouraged to communicate their observations to Deputy Comptroller and Auditor General (Accounts and Reports) who will examine and then take suitable action.

1.13. Responsibility for keeping the Manual up-to- date is that of Deputy Comptroller and Auditor General (Accounts and Reports) and the manual is to be reviewed every three years. As required, these revisions will be issued to all holders of the auditing manual.

1.14. Deputy Comptroller and Auditor General (Accounts and Reports) is also responsible for communicating the contents of the manual to staff and monitoring to ensure compliance with the manual.

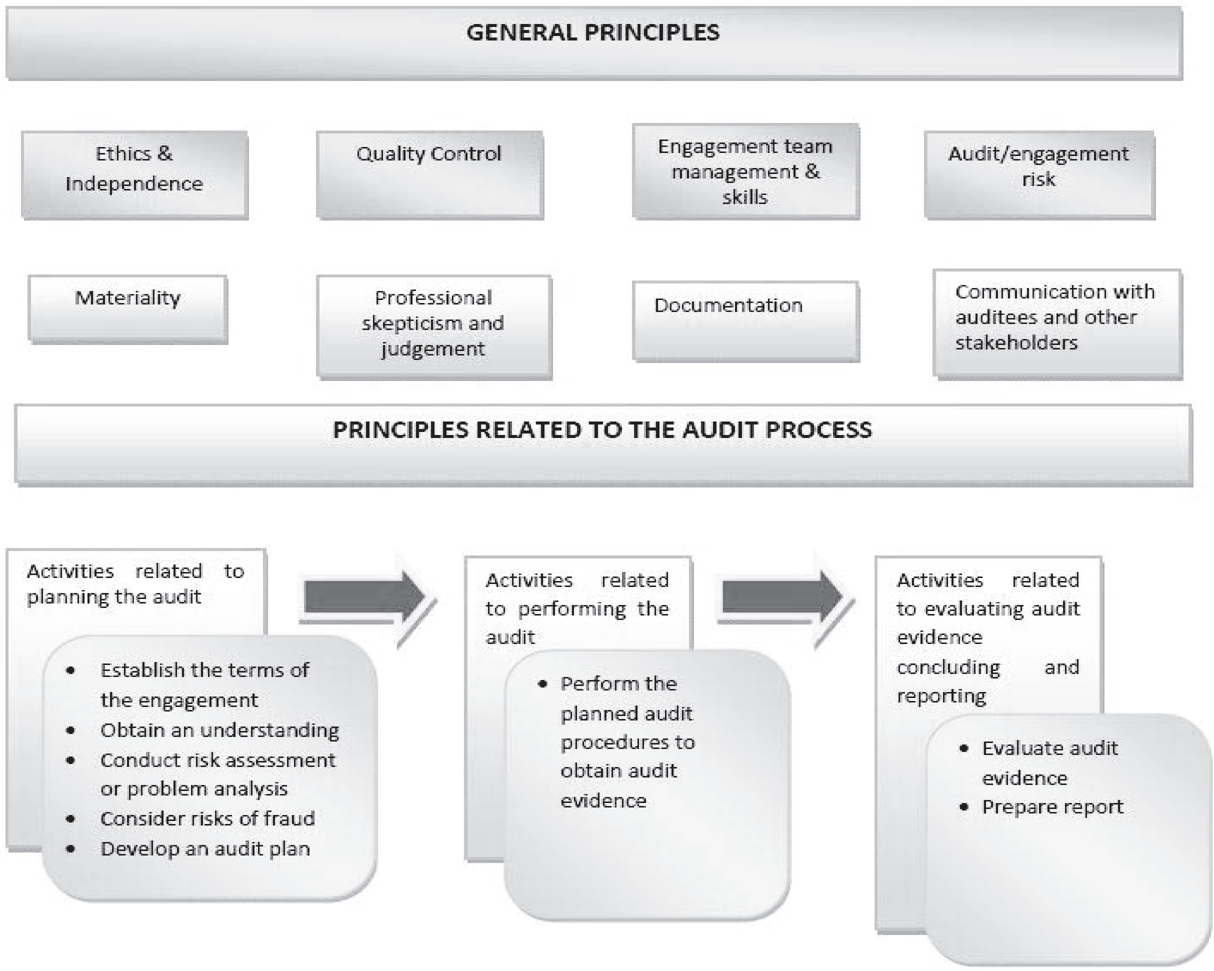
1.15. After brief details of the objective and scope of financial and compliance audit (Chapter 2), this manual covers the full audit cycle:

- Audit Planning (Chapter 3);
- Audit Fieldwork (Chapter 4); and
- Audit Reporting (Chapter 5).

1.16. More details on the general principles to be covered in an audit is given in Figure 1 below.

The General Principles

Figure 1: Principles to be applied in conducting an audit



Source: ISSAI 100 (Paragraph 34)

The above Figure deals with both general principles and principles related to the audit process. Chapter 1 of this Manual gives more details of the general principles and the rest of this manual gives more details on the principles related to the audit process.

Ethics and Independence

1.17. Auditors should comply with relevant ethical requirements and be independent. Ethic principles should be embodied in an auditor's behaviour. The SAIs ethical policies should address ethical requirements and emphasise the need for compliance by each individual auditor. Ethics ensure that the audit is conducted with a professional attitude. The key principles of ethics are integrity, objectivity, professional competence and due care, confidentiality and professional behaviour. Auditors should be honest, reliable and truthful when conducting an audit. Auditors should remain independent so that their opinions/conclusions/findings will be impartial and be seen as such by third parties. Independence is freedom from situations and relationships which could impair the auditor's objectivity. Independence is an attitude of mind and appearance. It safeguards the ability to perform an audit without being affected by influences that might compromise professional judgement. Auditors can find additional guidance in ISSAI 10-Mexico Declaration on SAI Independence as well as ISSAI 11- INTOSAI Guidelines and Good Practices related to SAI Independence and ISSAI 30 - Code of Ethics.

Quality Control

1.18. Auditors should perform the audit in accordance with professional standards on quality control. The SAI's quality control policies and procedures should comply with professional standards. The aim is to ensure that audits are performed to a consistently good quality. Quality control procedures should include matters such as the direction, review, supervision of the audit process and consulting and reaching decisions on difficult or contentious matters. Auditors can find additional guidance in ISSAI 40-Quality Control for SAIs.

Engagement Team Management and Skills

1.19. Auditors should possess or have access to the necessary skills. The individuals in the engagement team should collectively possess the knowledge, skills and expertise necessary to successfully complete the audit. This includes an understanding of and practical experience of the type of audit being undertaken; an understanding of the applicable standards and legislation; an understanding of the entity's operations; and the ability and experience to exercise professional judgement. Consistent for all audits are the needs for recruiting personnel with suitable qualifications, developing and training employees, the preparation of manuals and other written guidance and instructions concerning the conduct of audits, and the assignment of sufficient resources for the audit. Auditors should maintain professional competence through continuous professional development.

1.20. In circumstances where it is relevant or necessary and in line with its mandate, and applicable legislation the auditor may use the work of internal auditors, other auditors or experts. The auditor should perform procedures that provide a sufficient basis for using the work of others and in all cases the auditor should obtain evidence concerning the other auditor or expert's competence and independence. However, the SAI has sole responsibility for any audit opinion or report it might make on the subject matter and that responsibility is not reduced by its use of the work of others.

1.21. The objectives of internal audit are different from those of the external audit. However, both internal and external audit promote good governance through contributions to transparency and accountability for the use of public resources as well as to promote efficient, effective, and economic public administration. This offers opportunities for coordination and cooperation and the possibility of eliminating duplication of effort.

1.22. Some SAIs use the work of other auditors working at state, province, region, district or parish level within the country, or in public accounting firms where they have completed audit work related to the audit objective. These arrangements should be conducted under agreements or contracts which include conditions to ensure work is done in accordance with public sector auditing standards.

1.23. Auditors may require specialised techniques, methods or skills which are not available within the SAI. Experts may be used in different ways e.g. to provide knowledge or conduct specific work.

Due Professional Care

1.24. The auditor should plan and conduct the audit in an alert and diligent manner. Auditors should avoid any conduct that might discredit the auditor's work. Auditors should perform their duties in accordance with technical and professional standards. Supervision, coaching and review should be conducted throughout the audit process. This includes ensuring that the audit team members understand the assignment; ensuring that the work is carried out in accordance with the audit plan; addressing issues that arise during the audit and monitoring the progress of the audit team members.

Audit/Engagement Risk

1.25. Auditors should manage the risk of providing incorrect opinions/ conclusions/ recommendations. The audit should be performed to reduce or manage the risk that the auditor's opinion/conclusion/findings/recommendations may be inappropriate or that the audit may fail to add value, to an acceptable level. Audit risk may arise due to fraud or error or due to the context, complexity and political sensitivity of the underlying subject matter or the risk that audit objectives are not sufficiently focused or penetrating.

Materiality

1.26. Auditors should consider materiality or significance throughout the audit process. In performance audit, the term 'significant' is comparable to the term 'material' as used in the context of financial and compliance audit. Determining materiality or significance is a matter of professional judgement and is based on the auditor's interpretation of mandate and perception of the information needs of the users. Materiality or significance considerations are relevant to all audit engagements and affect the determination of the nature, timing and extent of audit procedures as well as evaluating the results of the audit. In general terms, a matter may be judged material if knowledge of it would be likely to influence the decisions of intended users. The concept of materiality recognises that some matters are important, either individually or in aggregate, and others are not. Materiality is often considered in terms of value but the inherent nature of characteristics of an item or a group of items may also render a matter material. This also includes regulatory requirements. In addition to materiality by value and by nature a matter may be material because of the context in which it occurs. Significance can be seen as the relative importance of subject matter in relation to policies, strategic plans, number of citizens, or stakeholders concerned, economic magnitude, consequences for the society, etc.

Professional Skepticism and Judgement

1.27. Auditors should maintain objectivity and appropriate professional behaviour. Professional skepticism and professional judgement are important throughout the audit engagement. These principles are based on the interaction of professional and behavioural characteristics that recognise the auditor's responsibility to carry out analyses and reach conclusions based on evidence collected whilst maintaining professional distance, open-mindedness, receptiveness to views and arguments, and an alert and questioning attitude. Professional judgement represents the application of collective knowledge, skills and experience to the audit process.

Documentation

1.28. Auditors should prepare audit documentation in sufficient detail to provide a clear understanding of work performed, evidence obtained and conclusions reached. Audit documentation should include the audit strategy and plan and record of procedures performed, and evidence obtained and should support the communicated results. Documentation should be in sufficient detail to enable an experienced auditor, having no previous connection to the audit, to understand from the audit documentation the nature, timing and extent and the results of procedures performed; the audit evidence obtained to support the auditor's conclusions and recommendations; and to record reasoning on all significant matters that required the exercise of professional judgement and related conclusions.

Communication with Auditees and Other Stakeholders

1.29. Auditors should ensure good communication with the auditee. It is essential that the auditee is well informed of the matters related to the audit. This is important in developing a constructive working relationship. This communication includes the responsibilities of the auditor for obtaining information relevant to the audit, the responsibilities of the different parties for the audit, an overview of the scope and timing of the audit, and providing management and those charged with governance with timely observations and findings throughout the audit. Determining the form, content and frequency of communication is a matter of professional judgement.

1.30. Auditors should establish effective lines of communication with all relevant stakeholders. The auditor should also establish effective communication with all relevant stakeholders including management, those charged with governance, experts in the field and other parties concerned as they may have information that could be useful in planning, conducting or reporting on the audit.

Appendices and Annexes to this Manual

1.31. In addition to the basic guidance in the manual there is detailed practitioners guidance in the Appendices and Annexes.

Chapter 2 Objective & Scope of Financial and Compliance Audit

2.1. There should be a clear statement of the objective and scope of each audit assignment carried out by or on behalf of OCAG.

2.2. One or more audit objectives (financial certification and/or compliance) should be defined for each element of an audit assignment. This objective is a statement of what is to be achieved by the audit.

2.3. ISSAI 100 provides standards and guidance for the following fields of public sector auditing:

- Financial audit focusing on determining whether an entity's financial information is presented in accordance with an applicable financial reporting framework (Accounts code/ forms prescribed by CAG). This is accomplished by obtaining sufficient appropriate audit evidence to enable the auditor to express an opinion on whether the financial information is free from material misstatement whether due to fraud or error. ISSAI 200 elaborates on this further; and
- Compliance audit focuses on whether a particular subject matter is in compliance with authorities identified as criteria. Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public-sector financial management and the conduct of public officials. Examples are given in Appendix 1 to this manual.

2.4. The audit scope is a statement of what areas will be examined by the audit, what work is to be done and what methodology is to be used to achieve the audit objective(s). This applies equally to financial and compliance audits.

Chapter 3 Audit Planning

Audit Strategy and Audit Plan

3.1. The auditor is required to document the overall audit strategy and audit plan, as well as significant changes to those documents made during the audit and the reasons for such changes (Paragraph 9 of ISSAI 1300 and paragraph 12 of ISA 300).

3.2. Good planning is of great importance to the success of an audit. Without it there is a real danger that auditors may fail to obtain sufficient, appropriate audit evidence to support the opinions on financial statements and conclusions reached for compliance audits. Inadequate planning may also result in less than efficient and timely audits.

3.3. Before planning commences, the auditor should prepare a client letter of engagement, or if one exists already review it to see if revision is required (e.g. there are changes to the audit scope). The new or revised letter of engagement should be sent to the client for information and necessary actions. At a minimum the letter of engagement should contain material under the following headings:

- Introduction;
- scope of the audit (mention ISSAIs);
- responsibilities of auditors - mention rights under Article 128(1) of the Constitution of Bangladesh/other;
- the audit process;
- client responsibilities;
- audit arrangements; and
- other matters.

3.4. An example template letter of engagement is at Annex A.2. This will need to be amended for the specific circumstances of an individual audit. For example in the case of a compliance audit, the specific laws and regulations that the audit will be testing compliance with should be detailed in the scope section.

3.5. The overall audit strategy as documented using the template at Annex A and audit plan to be documented on the planning section of the electronic working papers package should reflect the audit objectives (financial certification and/or compliance) and scope set for the audit assignment (refer chapter 2).

3.6. In establishing the overall audit strategy and audit plan, the auditor shall:

(a) Identify the characteristics of the audit that define its scope;
(b) Ascertain the reporting objectives of the audit to plan the timing of the audit and the nature of the communications required;

(c) Consider the factors that, in the auditor's professional judgement, are significant in directing the auditor's efforts;

(d) Consider the results of preliminary audit engagement activities and, where applicable, whether knowledge gained on other audits performed by the Director General for the entity is relevant; and

(e) Ascertain the nature, timing and extent of resources necessary to perform the audit.

3.7. The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:

- The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters;
- The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas;
- When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates; and
- How such resources are managed, directed and supervised, such as when team briefing and debriefing meetings are expected to be held, how Director General and manager reviews are expected to take place (for example, on-site or off-site), and whether to complete audit quality control reviews.

3.8. The Overall Audit Strategy (for internal purposes) should be held within the electronic working papers system. This will record the key decisions made in planning the audit and facilitate communication of significant matters to the audit team.

3.9. The format of the Overall Audit Strategy will vary depending upon the size and complexity of the audit and of the team structure. For simple audits, the Overall Audit Strategy may be communicated in a team planning meeting and recorded in the minutes of that meeting. For other audits, a memorandum setting out key decisions on scope, timing and conduct of the audit may be appropriate.

3.10. The Overall Audit Strategy guides the audit planning process, and so it is important to capture at this stage the Director General's expectations and concerns for the audit so that the audit can be planned to address them.

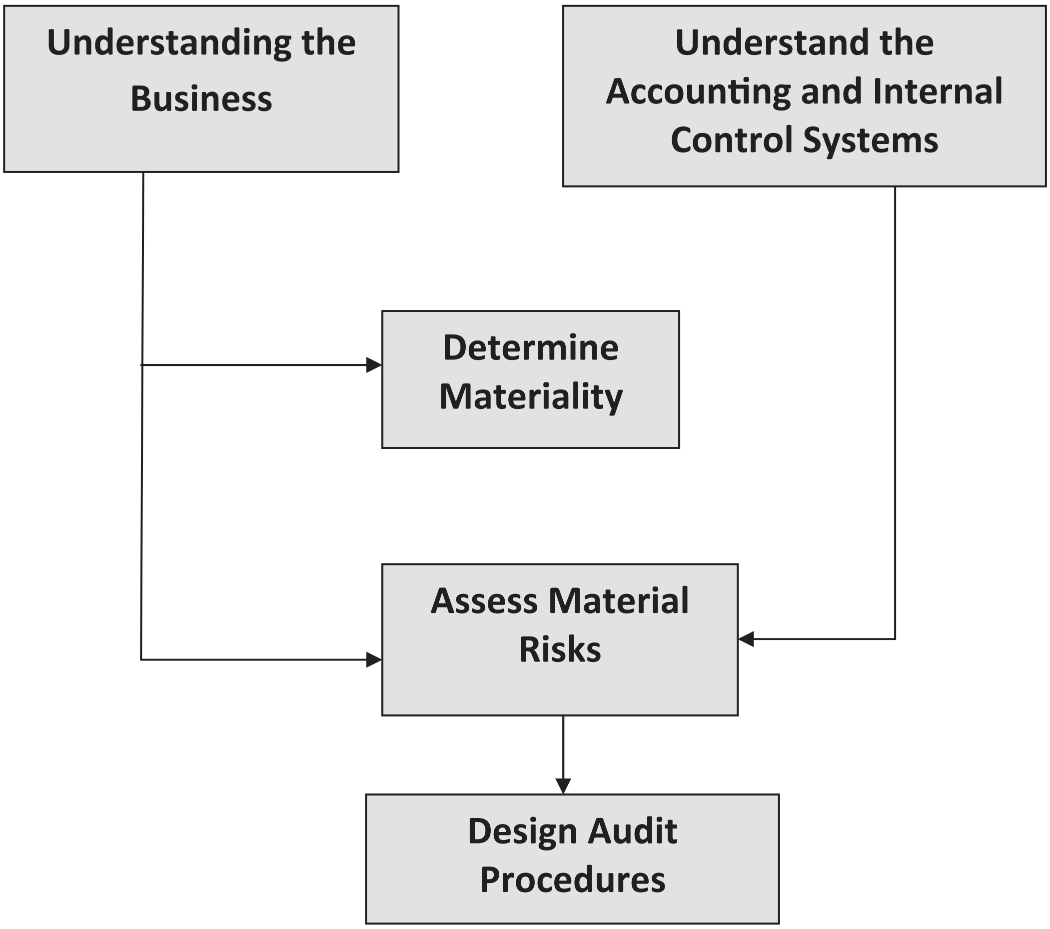
3.11. As part of developing the Overall Audit Strategy, the Director General will identify the required Risk Assessment Procedures. The audit team should ensure that they follow this planned approach, as the planning process will otherwise not have been effective or efficient.

3.12. In planning the audit, the auditor should ensure that all points identified in the Overall Audit Strategy flow through to the planned approach. Where detailed audit planning provides additional information, for example indicating that a possible risk identified in the Overall Audit Strategy is not relevant in the current year, the documentation should be revised, clearly set out the basis for this conclusion and, where relevant, the supporting audit evidence.

3.13. Any changes to the Overall Audit Strategy should be subject to the same level of review and approval as the original Overall Audit Strategy. The changes should be clearly documented in the electronic working papers. A formal consideration of the planning assumptions should be undertaken at the end of the development of the Audit Plan and at the end of the audit fieldwork stage.

3.14. To evidence that the necessary planning activities have occurred, the audit team should complete the Audit Planning checklist as per Annex A.1.

Figure 2: The Audit Process (1) - Key stages of audit planning



(For the Second stage of the audit process see Figure 5)

Understanding the Entity and its Environment

3.15. The auditor should gain adequate knowledge of the accountability framework and other external factors impacting on the client entity and use Annex B to document this. When completed electronically, Annex B should be loaded on to the Audit Management and Monitoring System (AMMS), the automated working papers system developed by OCAG, Bangladesh. Areas to document are:

1) Relevant industry, regulatory, and other external factors.(Ref: ISA 315 para A17-A22)

2) The nature of the entity and its operations (Ref: ISA 315 para A23-A27) - the purpose is to enable an understanding of the classes of transactions, account balances and disclosures to be expected in the financial statements.

3) The entity's financial reporting and accounting policies. (Ref: ISA 315 para A28)

4) The entity's objectives and strategies, and related business risks. (Ref: ISA 315 para A29-A35)

(5) The measurement and review of the entity's financial performance. (Ref: ISA 315 para A36-A41)

(6) The nature and extent of the entity's related party relationships. (Ref: ISA 550 para A11-A14).

(Note: Further guidance on understanding the entity for compliance auditing is given in Appendix 2 to this manual).

Understanding Entity's Internal Control

3.16. The auditor should complete the relevant section of Annex C to assess the strength of the Overall Control Environment, and use this form to evaluate the impact of any identified weakness on the assessment of inherent risk for individual audit areas. When completed electronically, Annex C should be loaded on to AMMS.

3.17. In documenting their understanding of internal control, the auditor should document the following 5 areas:

1) Control Environment (Ref: ISA 315 para A69-A78)

3.18. The purpose of understanding the control environment is to understand whether:

(a) Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical behaviour; and

(b) The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control, and whether those other components are not undermined by deficiencies in the control environment.

2) The entity's risk assessment process (Ref: ISA 315 para A79-A80)

3.19. Public sector bodies should have a risk assessment process, which should be appropriate for the size and complexity of the entity. The risk assessment process is involved in:

(a) Identifying business risks relevant to financial reporting objectives;

(b) Estimating the significance of the risks;

(c) Assessing the likelihood of their occurrence; and

(d) Deciding about actions to address those risks.

3) Monitoring of controls (Ref: ISA 315 para A98-104)

3.20. Monitoring of controls is a process to assess the effectiveness of internal control performance over time. It involves assessing the effectiveness of controls on a timely basis and taking necessary remedial actions. Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and include regular management and supervisory activities.

3.21. When completing this section of Annex C, the auditor should ensure that the following are considered:

(a) Any additional reporting responsibilities regarding internal controls;

(b) Relevant controls that relate to compliance with authorities;

(c) Controls related to monitoring performance against the budget;

(d) Controls related to transferring budgetary funds to other entities;

(e) Controls of classified data related to national security and sensitive personal data, such as tax and health information; and

(f) Supervision and other controls performed by parties outside the entity and relate to areas such as:

- Compliance with procurement regulations;
- Execution of the budget;
- Other areas as defined by legislation or audit mandate; and
- Management's accountability.

4) Business controls (Ref: ISA 315 para A81-A87)

3.22. The standing information for the audit of each entity should include systems notes for each class of transactions in the entity's operations that are significant to the financial statements, and for monitoring controls. The system notes should include:

- the procedures, within both information technology (IT) and manual systems, by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements. This should include how regularity is ensured;
- the related accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions. This includes the correction of incorrect information and how information is transferred to the general ledger. The records may be in either manual or electronic form; and
- how the information system captures events and conditions, other than transactions, that are significant to the financial statements.

3.23. System notes should clearly set out the flow of information within a business cycle, the IT systems involved, and where control activities and data interfaces take place (including controls over regularity). This can often be effectively documented using a system-flow diagram. The client or their internal audit team may have already prepared systems diagrams.

3.24. In addition to system notes on business cycles, the documentation should set out the financial reporting process used to prepare the entity's financial statements, including significant accounting estimates and disclosures, and the controls surrounding journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments.

5) The information system (Ref: ISA 315 para A81-A85)

3.25. The auditor should have sufficient understanding of the entity's information systems and their interaction with business controls (including controls over regularity) to be able to:

- identify any related risks of material misstatement or irregularity;
- identify where business controls are dependent upon general IT controls; and
- plan an effective and efficient audit.

3.26. Issues to consider when completing this section of Annex C are:

- Assessing the accounting systems
- Overall IT policy and strategy
- Development and maintenance
- Logical access security
- Physical control
- Computer Assisted Audit Techniques using IDEA software package.

3.27. The auditor should summarise the outcome of identification of IT risks and identification of controls dependent upon IT in Annex D. When completed electronically, Annex D should be loaded on to AMMS.

3.28. In completing Annex D, the Auditor should consider both impact and likelihood in considering whether there are risks of material misstatement or irregularity.

Risk Assessment

3.29. The Fraud Risk Assessment form at Annex E is designed to assist auditors in the evaluation of the potential risks of fraud in arriving at an assessment of the risk of material misstatement due to fraud. When completed electronically, Annex E should be loaded on to AMMS.

3.30. The auditor should evaluate whether the information obtained from the other risk assessment procedures and related activities performed indicates that one or more factors indicating potential risks are present. Whilst these factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and, therefore, may indicate risks of material misstatement due to fraud (ISA 240 para 24).

3.31. The auditor should identify and assess the risk of material misstatement due to fraud at the financial statement level (pervasive risks) and at the assertion level (significant risks and risk factors) for classes of transactions, account balances and disclosures (ISA 240 para 25).

3.32. For compliance audits, the auditor should assess whether there is a significant risk of non-compliance. To do this, the auditor should use judgement to evaluate relevant factors identified from the Risk Assessment Procedures including:

- the complexity of the regulations;
- the introduction of major new legislation or changes in existing regulations;
- services and programmes delivered through third parties; and
- payments and receipts made on the basis of claims or declarations.

3.33 Further guidance on assessing risk for compliance audits is given at Appendix 3.

3.34 The table below discusses further the features of Pervasive Risks, Specific Risks and Risk Factors, and comments on their impact on the audit approach.

Table 1 – Identification of and audit response to Pervasive and Specific risks and risk factors

	Pervasive Risk	Specific Risk	Risk Factor
Definition	A Significant Risk at the financial statement level that relates pervasively to the financial statements as a whole and potentially affects many assertions (for example the risk that a new accounting system does not work).	A Significant Risk at the assertion level (i.e. a Significant Risk which is not a Pervasive Risk). A Specific Risk will be a particular risk that can give rise to a material misstatement. There may be multiple related Specific Risks in relation to one audit area or a series of audit areas. For example the risk that the Public Procurement Rules are not followed in letting large public expenditure contracts – regularity assertion.	Risk Factors are either: • risks of material misstatement / irregularity which are addressed through a standard level of planned testing over the relevant assertions, and so do not require special audit consideration (for example the risk that amount paid exceeds the amount invoiced); or • potential risks which have been assessed as not representing a risk of material misstatement / irregularity and so do not require an audit response, but may require monitoring as the audit progresses (for example inventory overstated where inventory is not material). Risk Factors may include risks with an operational impact but without a direct impact on the financial statements.

	Pervasive Risk	Specific Risk	Risk Factor
Comments	Pervasive Risks are risk that do not directly relate to particular assertions for individual audit areas. Rather they represent circumstances that may increase the risk of material misstatement across audit areas, for example, through management override of internal control. Pervasive Risks are more likely to occur where there is a deficient control environment (although these risks may also relate to other factors, such as declining economic conditions). For example management's lack of competence may have a pervasive effect on the financial statements requiring an overall response by the auditor.	A Specific Risk means that there is a high risk of material misstatement in relation to a particular audit area. The auditor design audit procedures which are specifically responsive to the risk as this is the most effective and efficient way to obtain assurance that the audit area is not misstated. If the auditor did not design specifically responsive tests, he or she would either fail to address the risk at all, or need to perform substantially more testing to obtain sufficient appropriate audit evidence.	Where a potential risk is identified through the planning process or in the course of the audit, the auditor should clearly conclude on whether it requires special audit consideration, or whether it is a risk factor. Where it is a risk of material misstatement which is adequately addressed through a standard level of testing, the audit procedures which address the risk must be specified. Where a potential risk has been identified in the file and assessed as a risk factor (including a fraud risk factor), the auditor should clearly document the basis of this judgement. A business risk does not require a response as part of a financial audit unless it also involves a risk of material misstatement of the financial statements. A business risk could impact upon the financial statements by e.g., increasing costs through inflation in the costs of staffing, without this leading to a risk of misstatement.
Audit Response	The Audit Plan should include procedures to address the identified Pervasive Risks on an audit. These will typically consist of overall responses to address	The auditor should assess the design and implementation of the related controls and plan their audit	No additional audit procedures above a standard level of audit testing are required on risk factors, as they either do not represent

	Pervasive Risk	Specific Risk	Risk Factor
	the assessed risk of material misstatement at the financial statement level. The auditor should assess the design and implementation of the related controls and plan their audit approach to address this Significant Risk. Due to the nature of Pervasive Risks, there may not be mitigating controls, in which case the extent of the planned response should reflect the absence of controls assurance. As Pervasive Risks do not relate to specific Audit Areas or assertions, the audit response will not typically be in the form of substantive testing. Instead, overall responses may include: - emphasizing to the audit team the need to maintain professional scepticism; - assigning more experienced staff or those with special skills or using experts to the audit; - providing more supervision; - incorporating additional elements of unpredictability in the selection of further audit procedures to be performed; - where there are deficiencies in the control environment responding by making general	approach to address this Significant Risk. The auditor's response to Specific Risks should be to design and perform further audit procedures whose nature, timing, and extent are based on, and are responsive to, the assessed risks of material misstatement at the assertion level. The planned audit approach should consider the most effective and efficient way to address the risk. Where there are adequately designed and implemented controls, it may be most efficient to test the operating effectiveness of the controls mitigating the risk. Substantive audit tests should be tailored to address the risk directly, rather than simply increasing sample sizes using an Assurance Factor of 3 without further consideration of the most appropriate	a risk of material misstatement/irregularity, or are addressed by the standard level of planned work to gain assurance over each assertion. However, the auditor will usually keep in view the identified risk factors as part of maintaining an attitude of professional scepticism. In exceptional circumstances, the Director General or Director may determine in their professional judgement that it is appropriate to perform procedures in respect of a risk in order to: - address concerns raised by management or those charged with governance; - provide insights in the management letter as to how this risk may be addressed or identifying weaknesses in management's response; or - identify whether there are concerns that should be passed to client leads.

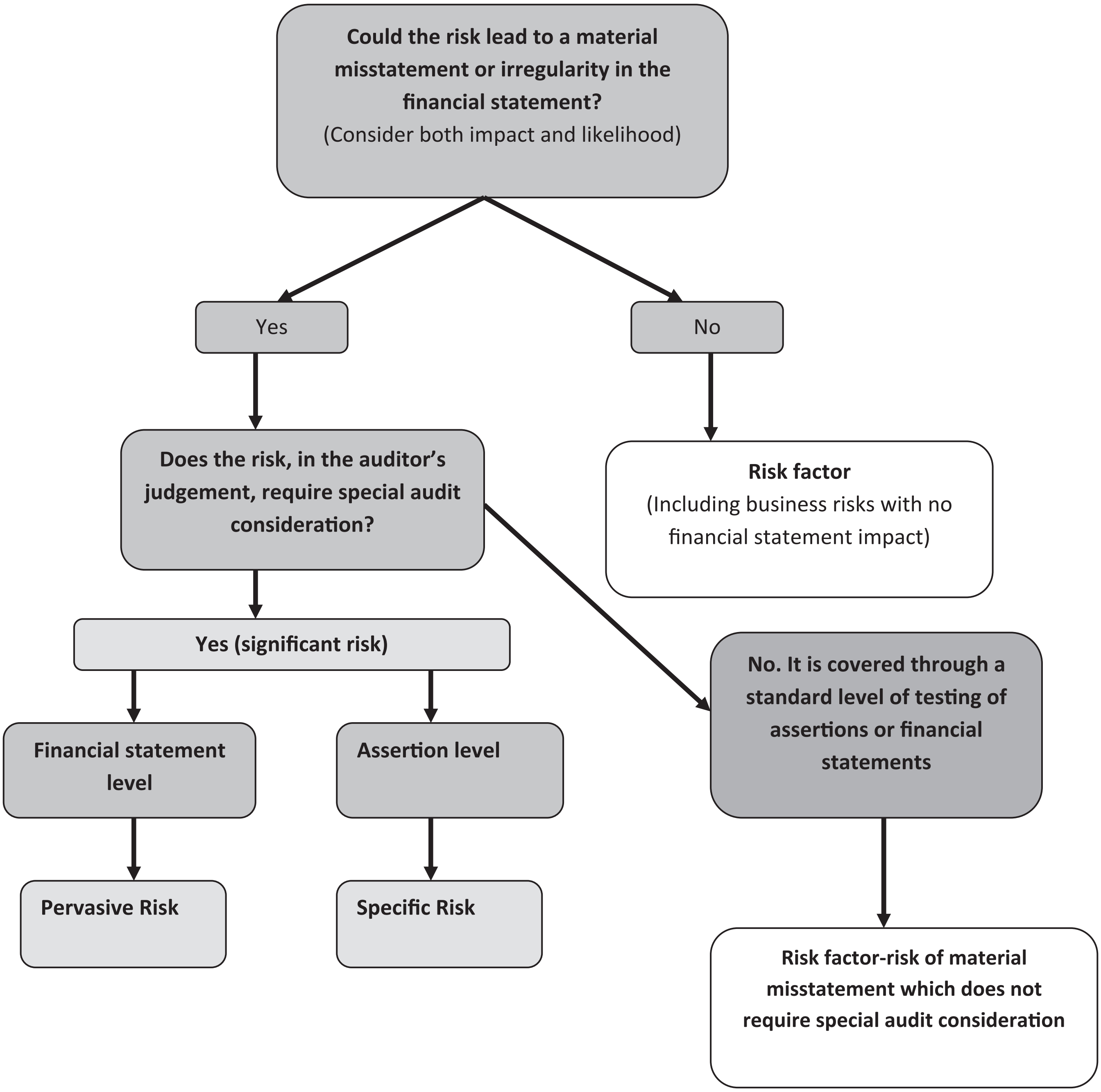
	Pervasive Risk	Specific Risk	Risk Factor
	changes to the nature, timing, or extent of audit procedures. For example conducting more audit procedures as at the period end rather than at an interim date, obtaining more extensive audit evidence from substantive procedures, or increasing the number of locations to be included in the audit scope; - independent review of the audit by a quality assurer; - increased testing of transactional controls as well as higher level controls; - procedures to address pervasive risks of fraud or error in an entity. For the example, Pervasive Risk that a new accounting system does not work, it would be appropriate for the auditor to carry out additional testing to confirm that balances have been carried correctly from old to new system, proper user acceptance testing (UAT) was successfully carried out by the entity on the new system in addition to the normal work of checking that the balances produced by the accounting system feed through correctly into the draft financial statements (which would be carried out whether the	audit response. For example, the auditor should consider relying on controls that ensure that the PPR are followed in expenditure (if such controls exist and are evidenced). If these controls are not in place or in place but not properly functioning, the auditor would also need to carry out additional testing of expenditure transactions focussed at perceived areas of greatest risk where the PPR are considered to be most likely to be broken (above and beyond the basic level of testing if compliance with the PPR were not considered to be a specific risk). Refer for more detail to the Procurement Audit Manual.	

	Pervasive Risk	Specific Risk	Risk Factor
	system was new or not).		

3.35. Examples of risk factors for compliance audits are given at Appendix 4 to this Manual.

3.36. The following decision tree summarises how potential risks are to be classified.

Figure 3: Classification of Potential Risks



3.37. The responses to Pervasive and Specific Risks should be clearly documented in the Significant Risks Testing Plan at Annex F (which should be completed electronically).

3.38. The audit approach to obtaining assurance over assertions for Audit Areas and over the financial statements should be documented in the Audit Area Testing Plan at Annex G (which should be completed electronically).

3.39. When the auditor has identified Risk Factors that do not require an audit response, they should document the reasons why they do not consider this to be a risk of material misstatement. This can be done in the Audit Area Testing Plan.

Materiality (ISSAI 1320)

3.40. After gathering relevant information to gain knowledge of the audited entity, the auditor needs to consider materiality, which is one of the key parameters that affect the audit strategy. The auditor needs to ensure that the audit efforts are concentrated on those areas and account components which are material.

3.41. Materiality is one of the basic and major concepts of auditing, central to planning and performing the audit, evaluating the effect of identified misstatements on the financial statements, and in forming the audit opinion. Materiality also provides preparers of financial statements with a basis for determining how transactions and balances should be disclosed and underlies professional standards on financial reporting. It is not possible for the auditor to form an opinion on financial statements without considering materiality.

3.42. Financial statements can rarely be absolutely correct and even if this were the case the user is unlikely to require this level of precision. A degree of tolerance in their accuracy is, therefore, accepted and this is recognized in the "properly presents", "presents fairly" and "true and fair" opinions that the auditor gives on most of the financial statements that he or she audits. Thus, materiality is defined as an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence.

3.43. The meaning of materiality as per ISA 320's general guidance :

- "misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;

- judgements about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and
- judgements about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered."

3.44. Materiality is a matter of professional judgement, and is affected by the perceived needs of the users of the financial statements. In considering the financial information need of users, the auditor can assume that users:

a) have a reasonable knowledge of business, accounting and economic activities and a willingness to study the information in the financial statements with reasonable diligence;
b) understand that financial statements are prepared, presented and audited to the levels of materiality;
c) recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
d) make reasonable economic decisions on the basis of the information in the financial statements.

3.45. Three types of materiality are explained in more detail at Annex H. They are:

- Materiality by value
- Materiality by nature
- Materiality by context

3.46. Annex H also introduces the concepts of performance materiality and expected error.

3.47. The materiality adopted for the audit at planning stage should be documented in the audit planning section of AMMS.

Analytical Procedures (ISSAI 1520)

3.48. Analytical procedures are the analysis of significant ratios and trends including the resulting investigation of fluctuations and relationships that are inconsistent with other relevant information or which deviate from predicted amounts.

3.49. Types of analytical procedure are explained in Annex I.

3.50. To carry out an effective audit the auditor must have a detailed knowledge of the business. A structured approach to planning including the use of analytical procedures helps to improve this knowledge. The auditor should apply analytical procedures at the planning stage to assist in understanding the entity's business in identifying areas of potentially high inherent risk and control risk and in planning the nature, timing and extent of other audit procedures.

3.51. Analytical procedures can be used in all audits at the planning stage to:

- confirm and improve their understanding of the organization's activities;
- identify areas of potentially high inherent risk and control risk;
- identify significant non-routine or unusual transactions and/or account balances;
- assist in planning the nature, timing and extent of substantive procedures including substantive analytical procedures.

3.52. The knowledge which the auditor gains from analytical procedure at the planning stage can be used to support the rest of the planning process and the development of the audit approach for the examination of specific account balances. Where analytical procedures used for planning reveal significant deviations from expectations the auditor will need to develop specific procedures to discover the cause of these fluctuations.

3.53. Analytical procedures at the planning stage may also involve a preliminary analysis of the available data in order to assist the auditor to decide whether substantive analytical procedures could be used to provide the required audit evidence at a reasonable cost. The auditor may, for example, carry out initial data analysis to assess the structure and quality of data and investigate possible relationships between variables.

3.54. The auditor will usually consider information from various sources both internal and external to the organization, when undertaking analytical procedures at the planning stage and at later stages. Typically, the auditor may consider information such as:

- prior year financial statements;
- appropriate external reports (e.g. performance and statistical reports);
- relevant non-financial information (e.g. staff numbers, claims processed);
- interim financial statements, reports and other analysis by the organisation's management comparing the current period results with prior periods and with current period budgets and forecast; and
- data on significant ratios and achievements against performance targets.

3.55. In many cases, auditors should be able to obtain much of this information from the organization's management.

3.56. The sophistication and extent of the analytical procedures applied at the planning stage are matters for the auditor's judgement and will vary depending on the size of the organization, its complexity and the availability of information. For some organizations the procedures may be limited to reviewing changes in account balances between the prior year and the current year. In other organizations the procedures might involve more extensive analysis of monthly financial statements and comparisons with non-financial data.

3.57. Analytical procedures used in planning that result in a better understanding of the transactions include:

- a review of the significant financial statement account balances and classes of transactions;
- a review of organization's budget and forecasts;
- a discussion on performance and future plans with finance and operational departments;
- an examination of statistics and other information about the organization's activities; and
- a review of achievement against budgets and performance targets.

3.58. These procedures will help the auditor to identify change in the organization's activities and operations which may affect its financial statements. They should also direct the auditor's attention to specific areas of the financial statements which require particular consideration.

3.59. With respect to the last bullet in paragraph 3.55, the auditor may wish to compare the actual amounts with the budgeted amounts. Analytical procedures, though, may not be very good at comparing budgets to actual as management may simply alter the actual to reflect the budget. Before placing too much reliance on this comparison, the auditor will need to assess the organization's budget setting procedures. In particular, the auditor should consider the pressures which may be placed on individual departments to conform to the budgets and the risk that results may be manipulated, for example, by the misallocation of expenditure between individual budget lines to ensure that budgets are met and appropriations are not exceeded.

3.60. Other analytical procedures that the auditor may employ as part of planning are trend and ratio analysis. For example, the auditor could plot the results from monthly management accounts to identify non-routine transactions and unexpected fluctuations which require explanation. Similarly, the auditor could perform ratio analysis such as:

- comparing commitments entered into as a percentage of total commitment appropriations made available to check the level of execution of the budget; and/or
- comparing actual monthly budgetary expenditure to budget which may show that a significant part of the expenditure is incurred during a holiday period, thereby indicating the possible existence of a problem.

3.61. Analytical procedures carried out at the planning stages should be documented on the planning section of AMMS.

Overall Audit Approach for Each Audit Area (ISSAI 1330)

The Audit Assurance Model

A. Background

3.62. In designing the audit plan, the overall objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

3.63. The planned audit procedures should be designed to obtain sufficient appropriate audit evidence through a combination of:

- Responding to Pervasive Risks to the financial statements;
- Responding to Specific Risks (relating to particular audit area assertions);
- Auditing Audit Areas (i.e. assertions not affected by Specific Risks); and
  Auditing the Financial Statements and reviewing other information.

B. Objectives

3.64. The objective of the auditor is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.

C. Relevant ISSAI and ISA guidance

3.65. The basic requirements which should be adhered to in respect of OCAG audits are contained in ISSAI 1330 and ISA 330 "The Auditor's Response to Assessed Risks", and ISSAI 1500 and ISA 500 "Audit Evidence".

3.66. All OCAG audits must comply with these standards. The guidance contained in this section emphasises the requirements of these standards and interprets the requirements in an OCAG context. Where relevant, the paragraphs cross-reference the application guidance in the ISSAIs and ISAs.

D. Core policies and guidance

3.67. The theory underpinning the OCAG methodology for auditing audit areas is designed to obtaining sufficient assurance to give a 95% confidence level that the financial statements are not materially misstated, i.e., the audit methodology is intended to reduce the audit risk (i.e. the risk of giving an incorrect audit opinion) to an acceptable level of less than a 5% chance.

3.68. This risk is made up of:

- the risk of there being errors in the financial statements; and
- the risk that the planned audit procedures would not detect any error that exists.

3.69. In order to keep the risk of an incorrect audit opinion to an acceptable level, the greater the risk of errors in the financial statements, the higher the level of assurance required from the planned audit procedures.

3.70. The required assurance is obtained by testing the assertions management have made about each significant Audit Area. Given the nature of the OCAG's role, the auditor's policy is also to obtain a minimum level of assurance over non-significant Audit Areas which is discussed further below.

Audit Assertions

3.71. In presenting the financial statements, management is making assertions about the information contained in them and the purpose of the audit is to test these assertions (i.e. the audit objectives are to obtain assurance over each of these assertions). The audit assertions which the auditor adopts are those included in Paragraph A11 of ISA 135. These are:

(a) Assertions about classes of transactions and events for the period under audit:

- **Occurrence**- transactions and events that have been recorded have actually been occurred and pertain to the entity. For example, for payroll an employee being paid by the entity is a bona fide employee.
- **Completeness**- all transactions and events that should have been recorded have been recorded. For example, for payroll that 12 months of transactions are posted to the ledger in the year of account.
- **Accuracy**- amounts and other data relating to recorded transactions and events have been recorded appropriately. For example:
  - the amount paid agrees to the invoice;
  - the correct amount was paid in accordance with the contract;
  - the invoice was checked against the purchase order and once the matching was satisfactory only then it was paid.
- **Cut-off** - transactions and events have been recorded in the correct accounting period. For example, a payment made on 30 June 2015 charged to the financial year ending 30 June 2015 and not the financial year ending 30 June 2016.
- **Classification**- transactions and events have been recorded in the proper accounts. For example, an item of income or expenditure is charged to the correct account/budget/economic code.

(b) Assertions about account balances at the period end:

- **Existence** - assets, liabilities, and equity interests exist. For example, a creditor balance is owed at the period end date and has not been paid before that date.
- **Rights and obligations** - the entity holds or controls the rights to assets, and liabilities are the obligations of the entity. For example, the audited entity holds title deeds for all tangible fixed assets included in land and buildings.
- **Completeness** - all assets, liabilities and equity interests that should have been recorded have been recorded. For example, tangible fixed assets include all land and buildings that the audited entity owns – none are excluded.
- **Valuation and allocation** - assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded. For example, the valuation of the audited entity's land and buildings has been revalued upwards to reflect the rising value of office buildings in the area where the entity has its HQ. The upwards valuation has resulted in a revaluation reserve.

(c) Assertions about presentation and disclosure:

- **Occurrence, rights and obligations** - disclosed events, transactions, and other matters have occurred and pertain to the entity. For example, contingent liabilities note includes only material cases that pertain to the entity.
- **Completeness** - all disclosures that should have been included in the financial statements have been included. For example, a related party's note should be included if required.
- **Classification and understandability**- financial information is appropriately presented and described, and disclosures are clearly expressed. For example, a segmental note reflects the way the audited entity is structured and significant allocation and apportionment methodologies are explained in the note.
- **Accuracy and valuation** - financial and other information are disclosed fairly and at appropriate amounts. For example, a contingent liability is disclosed in an account note on the basis that there is a high likelihood that a court case may be lost within the next year that would result in a payment being made. The estimated value is based on expert legal advice.

3.72. All the audit assertions listed at paragraph 3.69(a) above are relevant to the audit of Government Appropriation Accounts as these are prepared on the cash basis of accounting and only have expenditure. However, the Government Finance accounts have cash balances and borrowings and thus the assertions about cash balances at paragraph 3.69(b) are also relevant for the audit of the Government Finance Accounts. Assertions about presentation and disclosure at paragraph 3.69(c) are relevant for all financial audits.

3.73. The compliance audits carried out by the OCAG also give assurance on the regularity of transactions contained in the accounts. A transaction is considered to be regular if it is in accordance with:

- authorising legislation;
- regulations issued under governing legislation;
- Parliamentary authorities; and
- Treasury authorities.

3.74. The OCAG compliance audits also consider the propriety of transactions. Propriety covers the standards of conduct, behaviour and governance. It addresses issues such as fairness, integrity, the avoidance of waste and extravagance and open competition in the letting of contracts.

3.75. When determining the propriety of transactions the auditor should consider whether the entity has complied with the standards of conduct and behaviour expected of those charged with the management of public funds. This may be achieved by considering the arrangements in place at the client against generally accepted practice in the public sector or where necessary, drawing on precedents established following consideration of incidents by the Public Accounts Committee and guidance issued by other entities.

3.76. Propriety is not readily susceptible to objective verification and it is not expressly covered by the CAG's audit opinion. The auditor is not, therefore, required to undertake specific work in support of propriety. However, if an issue of propriety is identified during the course of audit work, the auditor must consider whether in their professional judgement the issue is of such significance that it needs to be reported to Parliament. This consideration should be documented in the electronic working papers.

The Audit Assurance Model for significant Audit Areas

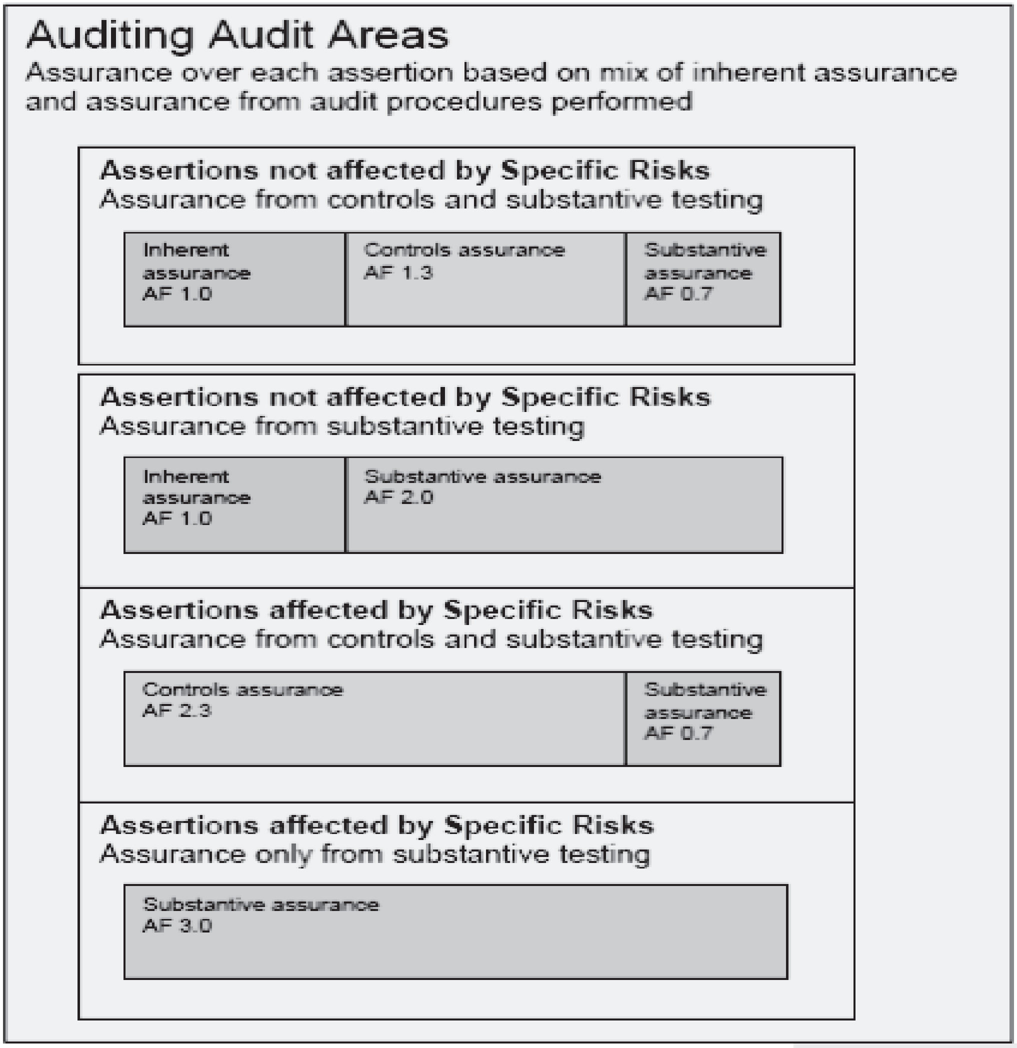
3.77. The planned audit procedures should provide assurance over each audit assertion for every significant class of transactions, account balances, or disclosures in the financial statements through a combination of inherent, controls and substantive assurance.

3.78. The statistical theory underpinning the OCAG audit methodology requires that to obtain 95% assurance, the sum of the Assurance Factors (AFs) from each source of assurance should be 3.0. This will be made up of a combination of:

- **Inherent assurance**: if a Specific Risk has been identified, then there is no inherent assurance (and greater controls and substantive assurance will be required totalling 3.0). If no Specific Risks has been identified, then there is inherent assurance, giving an AF of 1.0 (i.e. controls and substantive assurance only need to total an AF of 2.0).
- **Controls assurance**: audit procedures to test the operating effectiveness of controls that would prevent or detect an error in an audit assertion can provide controls assurance and reduce the substantive assurance required. Obtaining sufficient assurance over the operating effectiveness of controls mitigating Significant Risks (i.e. controls assurance of 2.3) requires more extensive controls testing than obtaining controls assurance of 1.3 from tests of controls over other assertions.
- **Substantive assurance**: the extent of substantive audit procedures required to obtain substantive assurance that an assertion is not materially misstated is affected by whether there are other sources of assurance available.

3.79. The diagram in next page shows how the sources of assurance interact in obtaining sufficient assurance.

Figure 4: Build-up of audit assurance over each audit assertion are shown in the diagram



Specific Risk for the relevant assertion	No	No	Yes	Yes
Testing shows that controls operating effectively over the relevant assertion	No	Yes	No	Yes
Basis of assurance				
Inherent Assurance	1.0	1.0	0.0	0.0
Controls Assurance	0.0	1.3	0.0	2.3
Substantive Assurance	2.0	0.7	3.0	0.7
Level of substantive testing	Standard	Basic	Focussed	Basic
Total	**3.0**	**3.0**	**3.0**	**3.0**

Note: Basic Substantive Procedures is the level of substantive procedures that should be planned if the auditor plans to take controls assurance over the assertion.

Standard Substantive Procedures: This is the level of substantive procedures that should be performed by the auditor if there are no Specific Risks over an assertion and a controls reliance approach has not been adopted.

Focused Substantive Procedures: This is the level of substantive procedures that should be performed by the auditor if they have identified a Specific Risk over an assertion, and either it is not planned to test controls or reliance cannot be placed on the controls due to inadequate design or unsuccessful controls testing.

3.80. The auditor should plan whether to rely on controls and substantive procedures, or substantive procedures alone, depending upon which approach is expected to be more effective in obtaining sufficient appropriate audit evidence. In making this decision, the auditor should also consider the efficiency of the planned approach (where effectiveness would not be affected).

3.81. Irrespective of the assessed risks of material misstatement identified in planning, the auditor should design and perform substantive procedures for each significant class of transactions, account balance, and disclosure. (Ref: ISA 330 para A42-A47)

3.82. The auditor should consider where it would be appropriate to use external confirmations as part of the substantive procedures, for example to request independent confirmations of bank balances. (Ref: ISA 330 para A48-A51)

3.83. Where there is a Specific Risk, the auditor should design tests which are specifically responsive to the risk, which is not necessarily achieved by simply increasing the scope of testing.

3.84. Performing "standard" audit tests with an increased sample size is often neither effective nor efficient to address Specific Risks – *"increasing the extent of an audit procedure is effective only if the audit procedure itself is relevant to the specific risk"* (ISA 330 para A15). Tailored audit tests and/or supplemental procedures are often more effective.

Example: Effective and ineffective responses to Specific Risks

The auditor has identified a Specific Risk of fraud through local finance staff maintaining "ghost employees" on the system after staff leave, and changing bank details to match their own. Extending standard audit tests would not necessarily provide assurance over this, as payments would appear to have been correctly processed. Using Computer Assisted Audit Techniques (CAATs) to identify examples of duplicate bank details or addresses among employees for follow-up, and using analytical procedures to identify if there were any locations with unusually low staff turnover, would address the Specific Risk directly.

Testing Non-significant Audit Areas

3.85. The ISAs only require substantive audit procedures be performed for classes of transactions, account balances, and disclosures that are material (i.e. significant Audit Areas). However, the auditor should plan to do a minimum level of substantive procedures on non-significant Audit Areas. This is below the level of testing that would be required for a significant Audit Area.

3.86. The auditor should consider whether the nature of balance means that additional audit procedures should be performed to gain assurance over any particular assertion.

3.87. If more complex tests are required to address an Audit Area, this may indicate that this is in fact a significant Audit Area.

3.88. Substantive analytical procedures can, if considered appropriate by the auditor, be based upon a comparison to prior year.

3.89. Tolerable error should be set at the lower of Performance Materiality or 25% of recorded amount (unless a lower tolerable difference is considered appropriate).

Example: auditing a non-significant revenue audit area

Interest receipts are a non-significant element of income at a total of Tk. 1 lac (prior year Tk. 1.2 lac) made up of receipts of interest during the year being audited from a number of fixed term bank deposits. The auditor has tested by agreeing the amount received to the trial balance and assessing its reasonableness against the average amount of money on deposit during the year and prevailing interest rates for fixed term deposits.

3.90. Tests of detail of non-significant Audit Areas do not have to cover all audit assertions unless considered necessary by the auditor. The planned procedures can be either an overstatement or understatement test i.e. either a sample of recorded items traced to supporting evidence, or a sample of items which would be expected to be recorded traced to the ledger (and so the test does not have to test for both occurrence and existence). Overstatement tests would typically be appropriate for debit items, and understatement tests for credit items.

Documenting the Audit Approach for Each Audit Area

3.91. The Audit Area Testing Plan at Annex G is to be used to provide a manageable means of viewing the audit approach for audit areas and to provide a means of documenting the sources of assurance. It is to be used in conjunction with the Significant Risks Testing Plan at Annex F to document how the auditor plans to achieve the planned level of assurance for each Audit Area. Both Annexes F and G should be completed electronically for each audit and loaded on to the planning section of AMMS to support the planned audit approach.

Decision Process for Planning Audit Approach to Audit Areas

3.92. The planned audit approach to each Audit Area should reflect the auditor’s consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence over each assertion through a combination of tests of controls and substantive procedures, or substantive procedures alone.

3.93. Tests of controls are designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. Designing tests of controls to obtain relevant audit evidence includes identifying conditions (characteristics or attributes) that indicate performance of a control, and deviation conditions which indicate departures from adequate performance. The auditor can then test the presence or absence of those conditions to determine whether the controls have operated effectively.

3.94. Substantive procedures are designed to detect material misstatements at the assertion level. Designing substantive procedures includes identifying conditions relevant to the purpose of the test that constitute a misstatement in the relevant assertion.

3.95. Substantive procedures can include substantive analytical procedures or tests of detail.

3.96. Selecting items to test through tests of detail may be done by a variety of methods, including testing 100% of items, testing specific items, and audit sampling.

Computer Assisted Audit Techniques

3.97. Computer Assisted Audit Techniques ('CAATs') describes a variety of methods of using information technology in audits, ranging from simple automation of checks such as casting of totals through to sophisticated analyses which would not be practical without using software.

3.98. The use of CAATs may enable 100% tests of electronic transactions and account files to be performed efficiently. This may be particularly useful in responding to Significant Risks.

3.99. CAATs can be used to select sample transactions from key electronic files, to sort transactions with specific characteristics, to test an entire population or to select a sample of transactions.

3.100. All OCAG auditors should have access to the main CAATs tool, IDEA. It is best practice to use a number of simple CAATs during audit testing to increase the effectiveness and efficiency of the work by the auditors e.g. replacing manual consistency checks.

3.101. Audit Team members should make use of IDEA where they judge it would be an effective substitute for equivalent manual procedures.

3.102. The auditor may also design CAATs as risk assessment procedures or audit tests to obtain assurance over assertions or address Significant Risks. CAATs can be used in risk assessment procedures or audit tests.

3.103. Any use of CAATs is dependent upon handling electronic data produced by the entity. All auditors should be aware of the need to respect and protect this data to hold it securely, only hold it for as long as is necessary, and dispose of it securely once it is no longer needed.

3.104. When using CAATs, the auditor should evaluate whether the information is sufficiently reliable for the purposes, including as necessary in the circumstances:

(a) obtaining audit evidence about the accuracy and completeness of the information; (Ref: ISA 500 para A49-A50) and

(b) evaluating whether the information is sufficiently precise and detailed for the auditor's purposes. (Ref: ISA 500 para A51)

3.105. Evidence about accuracy and completeness of information used in performing an audit procedure can be obtained concurrently as an integral part of the audit procedure itself, by testing controls over the preparation and maintenance of the information, or by additional audit procedures. For example, the auditor might check that the listing being used totals to the amount included in the trial balance, which, together with the tests performed as part of the CAATs, would give assurance over this.

3.106. Where CAATs are relied upon for substantive assurance the testing will include vouching back sample items selected to source documentation.

3.107. CAATs can be used to automate a number of audit procedures, such as:

- selection of statistically valid samples e.g. using Monetary Unit Sampling;
- reperforming calculations;
- reconciling the general ledger to sub-ledgers;
- recalculating totals or subtotals in files;
- analysing and summarising data (e.g. splitting into debits and credits);
- developing expectations for substantive analytical procedures;
- selection of items with particular characteristics in a balance.

3.108. CAATs can be effective as a tool for checking the accuracy and completeness of information taken from data sets the auditor is already testing for other purposes. For example, CAATs can be used to re-create the trial balance by performing summarisation of account code totals.

Using Computer Assisted Audit Techniques (CAATs) as Risk Assessment Procedures or as Audit Tests

3.109. As part of establishing the Overall Audit Strategy, the auditor should consider whether it would be effective and efficient to use Computer Assisted Audit Techniques as risk assessment procedures or as audit tests and document on the planning section of AMMS.

3.110. Examples of uses of CAATs as risk assessment procedures include:

- performing analyses to check what the client is telling us about the nature of transactions;
- performing preliminary analytical procedures, such as comparisons of outturn by location, or by types of expenditure; and
- summarising transactions with particular counterparties.

Common Examples of Using CAATs as an Audit Tests are in Journal Entry Testing and Profiling

3.111. Other examples of possible uses of CAATs as audit tests include:

- identifying duplicate payments;
- checking numeric/date sequences such as order or invoice numbers for gaps;
- comparing addresses or other information to identify employees that are also suppliers;
- comparing addresses or other information to identify possible ghost employees;
- identifying suppliers with only PO Boxes as addresses;
- sorting payments by value to identify transactions that fall just under authorisation limits;
- identifying unusual items e.g.:
  - employees working unusually high hours or at unusual rates;
  - unusually high or frequent expense claims;
  - unusual patterns in the level of usage of suppliers;
  - large round-sum items;
- checking data logs for modifications to master files; and
- checking for slow-moving inventory.

Journal Entry Testing

3.112. The auditor is required to test journal entries as part of their response to the Pervasive Risk of fraud through management override of controls.

3.113. When automated procedures are used to maintain the general ledger and prepare financial statements, journal entries may exist only in electronic form. It may, therefore, be most effective and efficient to use CAATs to test journal entries.

3.114. Where possible, IDEA should be used to identify journals of interest (in particular year-end journals) and selecting some (or, if higher risk, all) of those journals for testing. For example, IDEA can be used to identify:

. journals exceeding authorisation limits;

- journals raised by individuals raising few journals in the year;
- journals containing key-words such as “correction”, “error”, “fraud”, “write-off” etc; or
- journals posted to accounts of particular sensitivity.

Profiling

3.115. CAATs are usually necessary when the auditor uses profiling as a sampling technique for tests of detail. Profiling is a sampling technique which can be used where it is possible to identify characteristics of items within the population which would indicate whether or not they are likely to be of audit interest. Profiling involves stratifying population into items requiring differing levels of testing, focusing testing on the items most likely to be of audit interest while reducing the overall extent of the procedures performed.

Examples:

a) Divide the population of the non-payroll expenditure population into expenditure in each month of the year of account. This may indicate that there has been a year end surge of expenditure to use up the available budget. Audit testing might be focussed on the month when expenditure is maximum (presumably the last month in the year of account) with a focus on finding whether expenditure was bona fide and good value for money and not paid for in advance of need to use up the budget;

b) Divide the population of the non-payroll expenditure population into expenditure in each day of the week during the year of account. Extract the higher risk items of expenditure on weekend days. If it is not normal to spend money on a weekend, investigate a sample of weekend expenditure to confirm it is for bona fide business purposes and not personal expenditure.

Audit Programmes

3.116. An audit programme should be written for each audit area setting out the risks specific to the audit area (and potential consequences if the risk is realised), the objectives of the testing, and the audit tests required to reflect the planned audit approach. Each audit test in the audit programme should have the audit assertions that are being tested and have a space for the auditor(s) who have carried out the audit to sign to indicate that they have completed the test and a working paper reference for the details of the testing carried out (working paper and/or matrix of test results).

3.117. Each completed audit programme should, once the audit plan has been approved, be loaded on to AMMS to ensure that they are all completed as part of the audit.

3.118. Some examples of audit programmes are given at annexes J1 to J10.

3.119. Some examples of Compliance audit procedures for inclusion in audit programmes are given in Appendix 5.

Sampling (ISSAI 1530)

3.120. More details on sampling methodology and the OCAG policy on using sampling for both financial and compliance audits to extract samples for detailed testing are given at Annex K

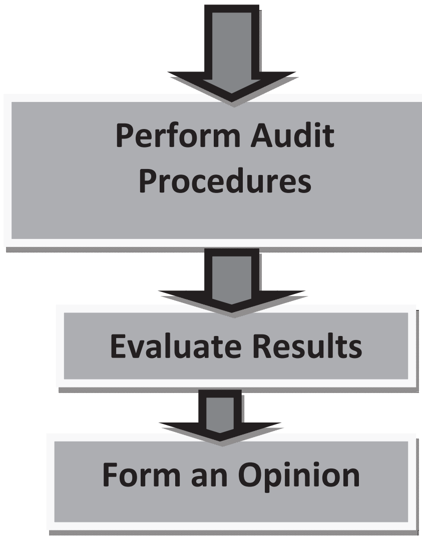
Quality Control Over Audit Fieldwork

3.121. All elements of planning completed by junior members of staff should be loaded on to AMMS and reviewed by a senior member of audit staff (most usually the team leader). The team leader is responsible for pulling together the planned audit approach, discussing it and agreeing it with the audited entity and the responsible Director General. The agreed audit approach should be summarised in a single document.

Chapter 4: Audit Fieldwork

Figure 5: The Audit Process (2) – Audit Procedures, Concluding and Reporting

(Continues from Figure 2 which shows the first stage in the audit process)



4.1. The auditor should design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence (ref: ISA 500 Para A1-A25). These audit procedures should be collated by audit area and included in audit programmes (see paragraphs 3.115 to 3.117) to ensure that all planned audit procedures are carried out.

4.2. The auditor can obtain audit evidence to draw reasonable conclusions on which to base the audit opinion (financial audit) or conclusions (for compliance audit) through performing:

- Risk Assessment Procedures to identify the risks that need to be addressed through the audit (see section in Audit Planning for more detail); and
- a combination of substantive and controls procedures.

4.3. Audit procedures to obtain audit evidence can include (individually or in combination):

- inspection;
- observation;
- confirmation;
- recalculation;
- reperformance; and
- analytical procedures (see Annex I).

4.4. These procedures are in addition to inquiry. Although inquiry may provide important audit evidence, and may even produce evidence of a misstatement, inquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls.

4.5. The sufficiency and appropriateness of audit evidence are interrelated. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.

4.6. Appropriateness is the measure of the quality of audit evidence i.e. whether it is relevant and reliable support for the conclusions on which the audit opinion (financial audit) or conclusions (for compliance audit) is based. The reliability of evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained. It is also important that audit evidence should be collected on a timely basis.

Example: Inter-relationship between quality of audit evidence and sufficiency

4.7. An issue has been identified over the terms of a side-agreement to a contract and what had been agreed with a supplier. A Specific Risk has been identified that management may be deliberately understating a liability or contingent liability associated with the contract. Inquiry of management and others involved in negotiating and managing the contract could provide extensive evidence in respect of this issue. However, this evidence may not be appropriate (given the nature of the risk identified) nor sufficient (as the quality of the evidence is poor in addressing a risk of deliberate misstatement). Extending the inquiries of more members of staff may not achieve sufficient assurance. A direct confirmation from the supplier to the Engagement Team, as part of a properly controlled confirmation process, would be high quality audit evidence that is appropriate in the circumstances. Unless there is a risk of collusion between management and the confirming supplier, a confirmation together with brief inquiry of a member of client staff may constitute sufficient appropriate audit evidence in the circumstances.

4.8. The Engagement Team should consider the relevance and reliability of the information to be used as audit evidence when designing and performing audit procedures. (Ref: ISA 500 para A26-A33)

4.9. Designing appropriate audit procedures involves identifying audit tests which provide relevant evidence.

4.10. Tests of controls are designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting material misstatements at the assertion level. Designing tests of controls to obtain relevant audit evidence includes identifying conditions (characteristics or attributes) that indicate performance of a control, and deviation conditions which indicate departures from adequate performance. The auditor can then test the presence or absence of those conditions to determine whether the controls have operated effectively.

4.11. Substantive procedures are designed to detect material misstatements at the assertion level. They comprise tests of detail and substantive analytical procedures. Designing substantive procedures includes identifying conditions relevant to the purpose of the test that constitute a misstatement in the relevant assertion.

4.12. Although it is difficult to generalise about what makes audit evidence more reliable, and there will be exceptions (for example, information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity), para A31 of ISA 500 notes the following general guidance on reliability of evidence:

- "The reliability of audit evidence is increased when it is obtained from independent sources outside the entity (for example, obtain a letter directly from the bank to confirm the audited entity's bank balance at the end of the year of account).
- The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective (for example audit evidence supporting the accuracy of expenditure by an organisation is increased when the auditor finds there are effective internal controls over the expenditure e.g., separation of duties in the procurement process, effective use of delegated financial authority limits, monthly reporting of totals vs budget profile to those charged with governance).
- Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
- Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).
- Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitised or otherwise transformed into electronic form, the reliability of

which may depend on the controls over their preparation and maintenance. For example, original invoices are better audit evidence than photocopies invoices as changes made manually before photocopying may be difficult to identify.

4.13. When designing tests of controls and tests of detail, the auditor shall determine means of selecting items for testing that are effective in meeting the purpose of the audit procedure (Ref: ISA 500 para A52-A56). This may be by:

- selecting all items (100% examination);
- selecting specific items; or
- audit sampling.

4.14. Guidance on the appropriate means of selecting items to test is included in Annex K.

4.15. When designing and performing substantive analytical procedures the auditor should determine the suitability of particular substantive analytical procedures for given assertions, taking into account of the assessed risks of material misstatement and tests of detail, if any, for these assertions. (Ref: ISA 520 para A6-A11)

4.16. If audit evidence obtained from different sources is inconsistent, or the auditor has doubts over the reliability of information to be used as audit evidence, the auditor should determine what modifications or additions to audit procedures are necessary to resolve the matter and consider the effect of the matter, if any, on other aspects of the audit. (Ref: ISA 500 para A57)

4.17. If, during audit testing or after reaching a conclusion, the auditor identifies information that is inconsistent with the final conclusion which the auditor has reached regarding a significant matter, the auditor should document how they have addressed the inconsistency. (Ref: ISA 230 para A15)

4.18. Unless the auditor has reason to believe the contrary, the auditor may accept records and documents as genuine. If conditions identified during the audit cause the auditor to believe that a document may not be authentic or that terms in a document have been modified but not disclosed to them, auditor should investigate further. (Ref: ISA 240 A9)

4.19. Possible procedures to investigate further may include:

- confirming directly with the third party; or
- using the work of an expert to assess the document's authenticity.

Use of Information Produced by the Entity

4.20. When using information produced by the entity, the auditor should evaluate whether the information is sufficiently reliable for their purposes, including as necessary in the circumstances:

a) obtaining audit evidence about the accuracy and completeness of the information; and (Ref: ISA 500 para A49-A50)

b) evaluating whether the information is sufficiently precise and detailed for the auditor's purposes. (Ref: ISA 500 para A51)

4.21. Audit evidence about the accuracy and completeness of information used in testing is necessary as the results of tests will be less reliable if they are based on inaccurate or incomplete data.

4.22. Evidence about accuracy and completeness of information used in performing an audit procedure can be obtained concurrently as an integral part of the audit procedure itself, by testing controls over the preparation and maintenance of the information, or by additional audit procedures.

Use of Information Prepared by Management's Experts

4.23. The preparation of the financial statements may require expertise in fields other than accounting or auditing, such as actuarial calculations, valuations or engineering data. Management may employ or engage experts to provide the necessary expertise.

4.24. Where information used in the audit has been prepared using the work of an expert employed or engaged by the entity, then the auditor should (Ref: ISA 500 para A34- A36):

- evaluate the competence, capabilities and objectivity of the expert; (Ref: ISA 500 para A37- A43)
- obtain an understanding of the work of the expert; (Ref: ISA 500 para A44-A47) and
- evaluate the appropriateness of the expert's work as audit evidence for the relevant assertion .(Ref: ISA 500 para A48)

4.25. The extent of the work required depends on how significant management's expert's work is in the context of the audit– i.e. the audit procedures should reflect the materiality and risks of the balance or transaction being materially misstated.

4.26. Where the entity has used an expert because of a need for expertise in a field other than accounting or auditing, the auditor should determine whether to use the work of an OCAG expert. (Ref: ISA 620 para A4-A9)

4.27. The nature, timing and extent of the audit procedures required may be affected by such matters as:

- the nature and complexity of the matter to which management's expert's work relates;
- the risks of material misstatement;
- the availability of alternative sources of audit evidence;
- the nature, scope and objectives of management's expert's work;

- whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services;
- the extent to which management can exercise control or influence over the work of management's expert;
- whether management's expert is subject to technical performance standards or other professional or industry requirements;
- the nature and extent of any controls within the entity over management's expert's work;
- the auditor's knowledge and experience of management's expert's field of expertise; and
- their previous experience of the work of that expert.

Competence, Capability and Objectivity of Management's Expert

4.28. The competence, capabilities and objectivity of management's expert should be evaluated to assess the reliability of information produced by the expert. In assessing this:

- competence relates to the nature and level of expertise of management's expert;
- capability relates the ability of management's expert to exercise that competence in the circumstances. Factors that influence capability may include, for example, geographic location, and the availability of time and resources; and
- objectivity relates to the possible effects that bias, conflict of interest or the influence of others may have on the professional or business judgement of management's expert.

4.29. Information can come from:

- personal experience with previous work of that expert;
- discussions with that expert;
- discussions with others who are familiar with that expert's work;
- knowledge of that expert's qualifications, membership of a professional body or industry association, license to practice, or other forms of external recognition;
- published papers or books written by that expert; or
- an OCAG expert, if any, who assists the auditor in obtaining sufficient appropriate audit evidence in respect to information produced by the management's expert.

4.30. Relevant factors to consider include:

- whether the expert's work is subject to technical performance standards or other professional or industry requirements, for example, ethical standards and other membership requirements of a professional body or industry association, accreditation standards of a licensing body, or requirements imposed by law or regulation;

- the relevance of management's expert's competence to the matter for which that expert's work will be used, including any areas of specialty within that expert's field;
- management's expert's competence with respect to relevant accounting requirements, for example, knowledge of assumptions and methods, including models where applicable, that are consistent with the financial reporting framework; and
- whether unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures indicate that it may be necessary to reconsider the initial evaluation of the competence, capabilities and objectivity of management's expert as the audit progresses.

4.31. Threats to objectivity can arise from a variety of sources:

- self-interest threats;
- advocacy threats;
- familiarity threats;
- self-review threats; and
- intimidation threats.

4.32. Safeguards may reduce such threats, and may be created either by external structures (for example, the management's expert's profession, legislation or regulation), or by the management's expert's work environment (for example, quality control policies and procedures).

4.33. Although safeguards cannot eliminate all threats to a management's expert's objectivity, threats such as intimidation threats may be of less significance to an expert engaged by the entity than to an expert employed by the entity, and the effectiveness of safeguards such as quality control policies and procedures may be greater. Because the threat to objectivity created by being an employee of the entity will always be present, an expert employed by the entity cannot ordinarily be regarded as being more likely to be objective than other employees.

4.34. When evaluating the objectivity of an expert engaged by the entity, it may be relevant to discuss with management and that expert any interests and relationships that may create threats to the expert's objectivity, and any applicable safeguards, including any professional requirements that apply to the expert; and to evaluate whether the safeguards are adequate. Interests and relationships creating threats may include:

- financial interests;
- business and personal relationships;
- provision of other services.

Obtaining an Understanding of the Work of the Management's Expert

4.35. Understanding the work of the management's expert includes obtaining an understanding of the relevant field of expertise.

4.36. An understanding of the relevant field of expertise may be obtained in conjunction with the determination of whether the auditors have the expertise to evaluate the work of the management's expert, or whether they need to involve an OCAG expert in the audit to be able to evaluate management's expert's work.

4.37. The auditor should obtain an understanding of:

- whether the expert's field has areas of specialty within it that are relevant to the audit, and whether the expert is familiar with that speciality;
- whether any professional or other standards, and regulatory or legal requirements apply to the experts work and whether these have been followed;
- what assumptions and methods are used by the management's expert, and whether they are generally accepted within the expert's field and appropriate for financial reporting purposes;
- the nature of internal and external data or information the expert uses; and
- if the expert is engaged by the entity, the terms of the engagement letter or other written agreement, including nature, scope and objectives of the work, the respective roles and responsibilities of management and the expert, and nature, timing and extent of communication between management and the expert. If the expert is employed by the entity, it is less likely there will be a written agreement of this kind. Inquiry of the expert and other members of management may be the most appropriate way to obtain the necessary understanding.

Evaluating the Appropriateness of the Management's Expert's Work

4.38. The auditor should evaluate the appropriateness of management's expert's work, including consideration of:

- the relevance and reasonableness of that expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;

- if that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; and
- if that expert's work involves significant use of source data the relevance, completeness, and accuracy of that source data.

Fieldwork for Audit Areas

4.39. The overall audit objective in performing testing is to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion. Designing and implementing appropriate responses to testing the assertions, management make about each Audit Area is a key element of obtaining this evidence.

4.40. As discussed in the Audit Assurance Model in section of Chapter 3, the overall OCAG financial audit approach is to obtain assurance over each audit assertion for significant classes of transactions, account balances, or disclosures in the financial statements through a combination of inherent, controls and substantive assurance. A mix of assurances may also be appropriate in a compliance audit, so the same sort of analysis may be appropriate.

4.41. If, based on the audit Risk Assessment Procedures, the auditor has not identified a Specific Risk over an assertion, then the auditor may have inherent assurance over that assertion. The auditor, therefore, requires less assurance from controls and substantive testing than they would if there were a Specific Risk over that assertion, as summarised below.

4.42. Note that if one assertion in respect of an Audit Area is affected by a Specific Risk, the auditor may still be able to take inherent assurance over other assertions i.e. a Specific Risk does not necessarily increase the required assurance from controls and substantive tests over all assertions in an Audit Area.

4.43. The nature, timing and extent of the planned audit procedures should be based on, and responsive to, the assessed risks of material misstatement for the Audit Area, i.e. the appropriate procedures to test a particular assertion will vary depending upon the nature of the balance.

Nature

4.44. The planned audit approach to address each assertion in respect of an Audit Area should reflect the Director General and Manager’s consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence. This may be through a combination of tests of controls and substantive procedures, or substantive procedures alone.

4.45. The auditor should design and perform controls and/or substantive audit procedures whose nature, timing, and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. (Ref: ISA 330 para A4-A8)

4.46. In designing the nature, timing and extent of the audit procedures to be performed, the auditor should consider what the risks are for the particular Audit Area which could lead to an error in respect of a particular assertion. This consideration should reflect the results of the Risk Assessment Procedures in respect of each assertion for the Audit Area, including the likelihood of material misstatement due to the particular characteristics of the relevant class of transactions, account balance, or disclosure. (Ref: ISA 330 para A9-A18)

4.47. The auditor should obtain more persuasive audit evidence higher than their assessment of risk. (Ref: ISA 330 para A19)

4.48. ISA 330 provides guidance on the meaning of nature, timing and extent of procedures, and notes that the nature of the audit procedures is the most important element of designing procedures which are responsive to the assessed risks of material misstatement:

- the nature of an audit procedure refers to its purpose (i.e. test of controls or substantive procedure) and its type (that is, inspection, observation, inquiry, confirmation, recalculation, reperformance, or analytical procedure);
- timing of an audit procedure refers to when it is performed, or the period or date to which the audit evidence applies;
- extent of an audit procedure refers to the quantity to be performed, for example, a sample size or the number of observations of a control activity.

4.49. As well as affecting the nature, timing and extent of the planned procedures, the risks identified may affect whether more than one procedure should be performed in combination.

4.50. For assertions not affected by Specific Risks, the auditor can obtain assurance from:

- Controls procedures together with Tests of detail (including CAATs or reliance on others);
- Controls procedures together with Substantive Analytic Procedures;
- Tests of detail alone (including CAATs or reliance on others); or
- Substantive Analytic Procedures alone.

4.51. The auditor should determine whether it is appropriate to plan to obtain assurance over an assertion from the entity's control activities.

4.52. If the auditor plans to rely on controls for assurance over particular assertions, then they should evaluate the design and implementation of the relevant control activities, and plan to test the operating effectiveness of the controls in the current period.

4.53. If auditor does not plan to rely on controls in respect of any assertions in an Audit Area, then they do not need to evaluate the design and implementation of any controls over that Audit Area or to perform any controls testing.

4.54. The auditor should consider whether external confirmation procedures are to be performed as substantive audit procedures. (Ref: ISA 330 para A48-A51)

Timing

4.55. The auditor should consider whether it is effective and efficient to perform audit procedures at an interim date, and perform "roll-forward" testing to the year-end.

4.56. The timing of audit procedures should reflect the nature of the risk affecting each assertion.

Extent

4.57. The auditor should determine the extent of the controls and substantive procedures required based upon the materiality, the assessed risk, and how much assurance they plan to obtain from each of controls and substantive assurance. Detailed guidance on how to determine the extent of testing is set out in the chapters on each testing approach.

Decision Process for Approach to Testing an Assertion

4.58. Selecting an appropriate audit approach for each assertion is important both in terms of delivering an effective audit, and also in terms of audit efficiency.

4.59. The nature of the planned procedures is the most important factor in ensuring that the auditor obtains appropriate assurance over each assertion. Increasing the extent of an audit procedure is effective only if the audit procedure itself is relevant to the risks over an assertion.

4.60. Parliament and the public generally expect public bodies to have effective controls in place to mitigate the risks that affect them. Therefore, the expectation should be that there are appropriately designed and implemented controls in place over most Audit Areas.

4.61. Where this is the case, it will usually be appropriate to test the operating effectiveness of relevant controls, and then to perform a basic level of substantive procedures.

4.62. This may be carried out through substantive analytical procedures, CAATs, around accounting estimates, or tests of detail:

- if using substantive analytical procedures, they should be predictive in nature and performed with a tolerable error that is the lower of Performance Materiality and 10-25% of the recorded amount (with the percentage set by the team using professional judgement).

- if using sample testing, the minimum sample size for tests of detail is 5 items, and Monetary Unit Sampling (MUS) is typically an appropriate sample selection method.

4.63. If appropriately designed and implemented controls are in place, but it is not effective and efficient to test the operating effectiveness of controls, then the auditor will need to perform a standard level of substantive procedures:

- if using sample testing, the minimum sample size for tests of detail is 5 items, and Monetary Unit Sampling (MUS) is typically an appropriate sample selection method; and
- if using substantive analytical procedures, the analytical procedures should be predictive in nature and performed with a tolerable error of (Materiality x SqRt (Recorded Amount/Materiality Base), capped at Performance Materiality.

4.64. The auditor should perform substantive procedures to obtain assurance over the financial statements, including:

a) agreeing or reconciling the financial statements with the underlying accounting records; and

b) examining material journal entries and other adjustments made during the course of preparing the financial statements. (Ref: ISA 330 para A52)

4.65. The procedures around year-end journal entries will normally be combined with the procedures performed in responding to the pervasive risk of management override of controls. If there is a specific year-end journal process, the auditor should ensure that the testing includes all material year-end journals.

4.66. In some accounting systems, year-end journals are reflected in an additional "Period 13" accounting period, or otherwise segregated within the accounting system. In other entities, adjustments may be posted directly in the preparation of the financial statements, without adjustments necessarily being reflected in the underlying records.

4.67. The nature and extent of procedures on journal entries and other adjustments in preparing the financial statements depends on the nature and complexity of the financial reporting close down the process and any risks identified.

4.68. It is usually most efficient for the final audit to begin after management have prepared a draft account. Example of procedures for agreeing financial statements to supporting records and examining journals and other adjustments are discussed below.

Auditing from a Draft Account: Procedures for Agreeing Financial Statements and Examining Journals and Other Adjustments

4.69. If the audit work on classes of transactions and account balances takes place after management have prepared a draft account, typically agreeing or reconciling the financial statements with the underlying accounting records will involve:

Before beginning testing as part of the year-end audit:

- obtaining management's mapping from the trial balance to the financial statements;
- checking that the mapping of individual lines to audit areas is appropriate;
- identifying adjustments between the trial balance and the draft account; and
- preparing lead schedules based upon the draft account.

In performing testing as part of the year-end audit:

- testing material journal entries in the preparation of the draft account (typically as part of responding to the pervasive risk of management override of controls);
- testing material adjustments between the trial balance and the draft account; and
- testing other journal entries and adjustments in the preparation of the draft account where appropriate (typically most adjustments in preparing the draft account will be tested)

In auditing the final financial statements:

- update lead schedules for adjustments between draft and final account;
- testing material journal entries between the draft and final account;
- testing material adjustments between the draft and final account; and
- testing other journal entries and adjustments in the preparation of the final account where appropriate (typically most adjustments in preparing the final account will be tested)

Assurance is, therefore, built up out of:

- audit of the draft account figures, including journal entries and other adjustments between the trial balance and draft account; and
- audit of adjustments between draft account and final account.

4.70. Where it is not possible/ practicable to audit from a draft account, it may be necessary to perform the audit work on classes of transactions and account balances from the trial balance and later perform procedures on the financial statements. This approach may also be appropriate in some circumstances when auditing components of groups to facilitate the consolidation process.

Evaluate Presentation and Disclosures

4.71. The auditor should perform audit procedures to evaluate whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework. (Ref: ISA 330 para A59)

4.72. This includes evaluating whether:

- the individual financial statements are presented in a manner that reflects the appropriate classification and description of financial information in accordance with the applicable financial reporting framework;
- the form, arrangement, and content of the financial statements and their appended notes are in accordance with the applicable financial reporting framework; and
- the terminologies used, the amount of detail given, the classification of items in the statements, and the accounting bases used are in accordance with the applicable financial reporting framework.

Information Accompanying the Financial Statements

4.73. The auditor should read information accompanying the financial statements that is not included in the financial statements and ensure it is consistent with the financial statements.

4.74. If, on reading the information, the auditor identifies a material inconsistency, the auditor should determine whether the audited financial statements or the other information needs to be revised.

4.75. If revision of the audited financial statements is necessary and management refuses to make the revision, the auditor should modify the opinion in the audit report.

4.76. If revision of the information is necessary and management refuses to make the revision, the auditor should:

a) include in the audit report an Other Matter(s) paragraph describing the material inconsistency;
b) withhold the audit report; or
c) withdraw from the audit engagement where possible.

4.77. The Engagement Team should document in the electronic working paper file the work performed in auditing the financial statements and disclosures. The Audit Area Testing Plan (Annex G) includes space to document the planned procedures.

4.78. The electronic working paper file should demonstrate that the financial statements agree or reconcile with the underlying accounting records.

4.79. The documentation on the electronic working paper file should include a referenced and tied in version of the final financial statements.

4.80. A clear audit trail between initial audit work and the final account, including clear documentation of how adjustments have been audited, is important in evidencing that the audit opinion is appropriately supported.

4.81. The lead schedule adjustment columns provide a useful mechanism for documenting this (see template lead schedule at Annex L).

4.82. The electronic working paper file documentation should include:

a) the results of those procedures performed to assess whether the information in the material to be published with the financial statements is consistent with the financial statements, including details of any material inconsistencies identified and how they were resolved; and

b) the conclusion reached as to whether the information in the material to be published with the financial statements is consistent with the financial statements.

Testing Controls

4.83. See Annex M for detailed guidance on how the testing of controls should be conducted and documented, including guidance on sample sizes for different tests of control. For both financial and compliance audits, controls testing carried out should be fully documented on AMMS, along with recommendations for improvement in cases where control were either found to be absent or found to be present but ineffective or not documented properly.

Tests of Detail

Background

4.84. 'Tests of detail' are substantive audit procedures which do not involve analytical review.

4.85. Tests of detail can include:

- 100% tests, covering every item in a population;
- Computer Assisted Audit Techniques, focussing testing on relevant items in the population; or
- audit sampling.

4.86. The procedures performed may include:

- physical examination;
- vouching;
- recalculation;
- confirmation of individual items or transactions;
- observation; and
- inspection.

4.87. Appropriately designed tests of detail can provide sufficient appropriate audit evidence to provide all of the assurance over an assertion, including when there is a Specific Risk.

4.88. Tests of detail may also be combined with tests of control or substantive analytic procedures to provide the overall planned assurance.

4.89. Tests of detail and analytical procedures carried out should be documented in working papers and/or matrices of test results and the completed working paper(s) should be loaded on to AMMS.

Relevant ISA/ISSAIs and Other Guidance

4.90. The basic requirements which should be adhered to in respect of OCAG audits are contained in International Standards on Auditing (ISAs). The main requirements and guidance which impacts upon this area of the audit are contained in ISA 330 "The Auditor's Response to Assessed Risks", ISA 500 "Audit Evidence", and ISA 530 "Audit Sampling".

4.91. All OCAG audits must comply with these standards. The guidance contained here emphasises the requirements of these standards and interprets the requirements in an OCAG context. Where relevant, the paragraphs cross-reference the application guidance in the ISAs.

Core Policies and Guidance

Uses for Tests of Detail

4.92. The planned audit approach to each Audit Area should reflect the auditor's consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence over each assertion through a combination of tests of controls and substantive procedures, or substantive procedures alone.

4.93. Where Tests of Detail are an effective and efficient source of substantive assurance, the auditor should plan to use them as the substantive procedures required by ISA 330.

4.94. Depending upon the entity's circumstances, appropriately designed Tests of Detail may provide substantive assurance over any assertion or Audit Area.

4.95. Although it may be possible to obtain all assurance over an assertion from Tests of Detail, the auditor should consider whether it is more effective and efficient to perform testing in combination with Tests of Controls or Substantive Analytical Procedures.

4.96. Where there is a Specific Risk, although the auditor cannot obtain all assurance from Substantive Analytical Procedures, it may be effective and efficient to obtain the assurance through a combination of Tests of Detail and Substantive Analytical Procedures.

4.97. Where this is the case, the auditor may perform Tests of Detail with an Assurance Factor[1] (AF) of 1.0 and Substantive Analytic Procedures with an AF of 2.0, or Tests of Detail with an AF of 2.3 and Substantive Analytic Procedures with an AF of 0.7.

4.98. Although using both Substantive Analytical Procedures and tests of detail require teams to perform two separate tests, this will often provide high quality audit evidence through providing assurance from both analysis vs. appropriately generated expectations, and tests of underlying transactions.

4.99. The planned approach should reflect the most effective and efficient approach to obtaining the planned levels of assurance.

4.100. The appropriateness of testing an assertion through Tests of Detail (and through any particular test) is dependent upon a number of factors including:

- the nature of the entity and its operations;
- the auditor's knowledge of the client, gained from previous years' audits or auditing similar entities;
- The assessment of the risks of material misstatement, including whether there is a Specific Risk in respect of the assertion and the assessment of the risk of fraud;
- the reliability of the control environment;
- the risk of management override of controls;
- the extent to which assurance over multiple assurances can be obtained at the same time;
- the need to incorporate an element of unpredictability into the testing;
- the availability of financial and non-financial data from internal and external sources to enable testing including whether information is available to perform CAATs; and
- the relative cost-effectiveness of undertaking tests of detail compared with other means of obtaining evidence.

Planning and Performing Tests of Detail

Determine whether it is appropriate to use Tests of Detail

4.101. In planning whether to use Tests of Detail for an Audit Area, the auditor should determine the suitability of particular Tests of Detail for each assertion, taking account of the assessed risks of material misstatement and tests of controls, if any, for these assertions. (Ref: ISA 520 para A6-A11)

4.102. Auditors should only plan to rely on Tests of Detail if they are an effective and efficient means of obtaining audit evidence.

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[1] Assurance factors must add to 3.0 and show the planned balance between inherent assurance, controls assurance and substantive assurance.

4.103. It may be appropriate to combine tests of detail with substantive analytical procedures to obtain the overall planned level of assurance.

4.104. Substantive analytical procedures are in general an effective and efficient source of audit evidence over large volumes of transactions which tend to be predictable over time.

4.105. In particular, auditors should not assume that Tests of Detail based on large sample sizes will automatically provide a high level of assurance as the assurance achieved depends upon the nature and timing of the procedures performed, as well as their extent.

Determining how to Select Items for Testing

4.106. The auditor should determine means of selecting items for Tests of Detail that are effective in meeting the purpose of the audit procedure. (Ref: ISA 500 para A52-A56)

4.107. There are three main selection methods available for Tests of Detail:

- **100% testing** - where all transactions in the population or account balance are tested. This may be appropriate where, for example:
    - the population constitutes a small number of large value items, and so it is time-efficient;
    - there is a Specific Risk and other means do not provide sufficient appropriate audit evidence; or
    - the repetitive nature of a calculation or other process performed automatically by an information system makes a 100% examination cost effective.
- **Selecting specific items** - the auditor may decide that, based on their understanding of the entity, assessed risks of material misstatement, and characteristics of the population, the auditor wish to judgementally select specific items within the population to obtain assurance. Specific items selected may include:
    - ***High value or key items*.** Items where their high value, or with some other characteristic, for example, items that are suspicious, unusual, particularly risk-prone or that have a history of error, are selected.
    - ***All items over a certain amount***. The auditor may decide to examine items whose recorded values exceed a certain amount so as to verify a large proportion of the total amount of a class of transactions or account balance.
    - ***Items to obtain information***. The auditor may examine items to obtain information about matters such as the nature of the entity or the nature of transactions.

  Selecting specific items for testing is a non-statistical sampling approach, and will normally provide sufficient assurance over an assertion only where the auditor is able to conclude and document that there is not a risk of material misstatement in respect of other items in the population, as it does not provide assurance over items which have not been selected.

Selecting specific items may be appropriate for addressing a Specific Risk, where the auditor can select all items with characteristics of interest.

- **Audit Sampling -** ISA 530 defines sampling as "The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population." Audit sampling usually involves statistical sampling (although a non-statistical sample where all items have a chance of selection would also enable us to draw conclusions about the whole population).

  If the auditor decides to use audit sampling as an approach, in designing the sample approach, the auditor should consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn. (Ref: ISA 530 para A4-A9)

  Methods of Sample Selection are:

  Monetary Unit Sampling (MUS) - this is a method where the higher the value of a transaction or balance, the more likely it is to be selected.

  Judgemental Sampling - this is a method where the sample size is set judgementally, rather than on statistical grounds. In order to provide assurance over an assertion, the sampling method should give each item in the population a chance of selection.

  Profiling - under this method the population is first divided into discrete sub-populations with share characteristics which may be of audit interest. Sampling can then be carried out in each sub-population. To use this method a good knowledge of the account area is required.

  Simple Random Sampling (for high error rate balances) - the main characteristic of this method is that every transaction has the same chance of being included in the sample.

4.108. Detailed guidance on when each approach is appropriate is set out in Annex K.

4.109. In planning Tests of Detail, the auditor should consider the appropriate direction(s) of testing to obtain assurance over an assertion. For example, tests of detail related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.

4.110. On the other hand, tests of detail related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence.

not occur in reality/were falsified), so the auditor adds an 'Overstatement test' to the audit programme. He or she will typically select a sample of transactions from a listing of all recorded amounts, and the direction of the testing would be that he or she would check from the recorded amounts for the sample of transactions to supporting information.

4.113. By contrast, for the completeness assertion, the auditors require assurance that the expenditure or receipts are not understated (as the list is not complete). Therefore, in this case, the auditor would seek to select their sample from the source population, e.g. for expenditure the source population might be all payments as detailed on the bank statement or cash book, and the auditor might add a test in their audit programme to check for a sample of payment transactions that the auditor select from the bank statement that they are properly recorded in the listing of payments made that the auditor is testing as part of the audit. Different tests are likely to be needed for completeness of income, as there is a higher risk with cash receipts that all or part of the receipt is misappropriated and never enters the bank account or the listing of receipts.

Determining the Planned Audit Tests

4.114. The appropriateness of a test to obtaining the planned level of assurance depends upon the nature, timing and extent of the procedures performed.

4.115. The auditor should design appropriate procedures based upon:

(a) consideration of the reasons for the assessment given to the risk of material misstatement for each assertion, including the likelihood of material misstatement due to the particular characteristics of the Audit Area; and whether the auditor has controls assurance; (Ref: ISA 330 para A9-A18)

(b) planning to obtain more persuasive audit evidence, the higher the Engagement Team's assessment of risk. (Ref: ISA 330 para A19)

4.116. The auditor may obtain more persuasive evidence by increasing the quantity of the evidence through more extensive testing, or by obtaining evidence that is more relevant or reliable, for example, by placing more emphasis on obtaining third party evidence.

4.117. The members of the audit team designing and performing the procedures should have a clear understanding of what would constitute a misstatement so that the results of the procedures can be appropriately evaluated.

4.118. If the auditor has identified a Specific Risk, he or she should plan and perform procedures that are specifically responsive to that risk.

Nature

4.119. A test only provides assurance over an assertion if the nature of the test is appropriate. For example:

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Nature

4.119. A test only provides assurance over an assertion if the nature of the test is appropriate. For example:

- inspection of documents evidencing existence of an asset (such as a share certificate) may not provide assurance over ownership or valuation.
- inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets.
- evidence of post year-end receipt of payment on a debtor may evidence valuation, but not that it was a debtor of the entity at the balance sheet date (i.e. cut-off).

4.120. Possible tests of detail include:

- **External Confirmation** - This is a specific type of enquiry, where representation of information is obtained directly from a third party. A bank certificate giving details of a bank balance at a specific date is an example of confirmation evidence.
- **Recalculation** - This involves checking the mathematical accuracy of documents or records. Recalculation can be performed through the use of information technology, for example, by obtaining an electronic file from the entity and using CAATS to check the accuracy of the summarisation of the file.
- **Inspection** - Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

4.121. Other means of obtaining audit evidence are reperformance, observation and enquiry. In general, these are not appropriate for tests of detail:

- **Re-performance** - independently executing procedures that were originally performed as, e.g., part of the client's internal control. This may be done manually or through the use of CAATS.
- **Observation** - looking at a process or procedure being performed by others. Examples include the observation of the performance of control activities and observation of the counting of inventory by the client staff. Observation provides audit evidence about the performance of a process or procedure, but it is limited to the point in time at which the observation takes place.
- **Enquiry** - seeking information from knowledgeable persons, both financial and non-financial, within and outside the client's organisation. Enquiry alone ordinarily does not provide sufficient audit evidence and it should, therefore, be supported with corroboration.

4.122. The ISAs specifically require the auditor to consider for each audit whether external confirmation procedures should be performed. (Ref: ISA 330 para A48-A51)

4.123. Accordingly, in planning tests of detail the auditor should consider whether there are any assertions which external confirmations would be particularly appropriate to test. The auditor can confirm bank balances and other information relevant to banking relationships, but it may be appropriate to obtain confirmations of:

- the terms of agreements, contracts, or transactions between an entity and other parties, including the absence of certain conditions or side agreements;
- accounts receivable balances and terms;
- property title deeds held by lawyers for safe custody or as security;
- amounts due to lenders, including relevant terms of repayment and restrictive covenants; or
- accounts payable balances and terms.

Timing

4.124. Tests of detail may be performed at an interim date or at the period end.

4.125. The higher the risk of material misstatement, the more likely it is that the auditor may decide it is more effective to perform substantive procedures nearer to, or at the period end rather than at an earlier date, or to perform audit procedures unannounced or at unpredictable times (for example, performing audit procedures at selected locations on an unannounced basis). This is particularly relevant when considering the response to the risks of fraud.

Example: Risk of fraud affecting timing of work

The auditor has identified a number of factors which indicate a Specific Risk of management understating expenditure to avoid overspend against budget. The majority of testing had historically been performed at an interim stage, with procedures at year-end to roll-forward testing to year-end. However, due to the nature of the risk identified, the auditor concluded that it would not be effective to rely on a roll-forward of completeness testing. All work on completeness of liabilities was performed at year-end.

4.126. However, performing tests at an interim date may enable us to identify significant matters at an early stage. This enables us to resolve them with the assistance of management, or to develop an effective audit approach to address the issue.

4.127. Certain audit procedures can be performed only at or after the period end, for example:

- agreeing the financial statements to the accounting records;
- examining adjustments made during the course of preparing the financial statements; and

- procedures to respond to a risk that, at the period end, the entity may have entered into improper payments in advance of need, or transactions may not have been finalised.

4.128. Other factors that influence the auditor's consideration of when to perform audit procedures include:

- the control environment (as a strong control environment supports performing work at an interim date);
- when relevant information is available (for example, electronic files may subsequently be overwritten, or procedures to be observed may occur only at certain times);
- the nature of the risk (for example, if there is a risk of manipulation of the inventory balance, the auditor may wish to attend a year-end inventory count); and
- the period or date to which the audit evidence being tested relates.

Extent

4.129. The extent of the procedures performed should reflect materiality, the assessed risk, and the degree of assurance the auditor plans to obtain.

4.130. In general, the extent of audit procedures increases as the risk of material misstatement increases. However, increasing the extent of an audit procedure is effective only if the audit procedure itself is relevant to the specific risk.

4.131. The use of Computer Assisted Audit Techniques (CAATs) may enable more extensive testing of electronic transactions and account files, which may be useful to enable more extensive testing in response to a risk of fraud or material error. Such techniques can be used to select sample transactions from key electronic files to sort transactions with specific characteristics, or to test an entire population instead of a sample.

Documentation of Audit Fieldwork

4.132. All audit fieldwork carried out should be fully documented on working papers and/or matrices of test results which should be loaded on to AMMS and cross referred to audit programmes (referred to at paragraphs 3.115 to 3.117) with a statement as to whether the planned assurance towards the audit assertion or assertions has been obtained, or if not what additional work is to be carried out and/or reference to consequence for the audit opinion. Any finding (e.g. error or control weakness) should be fully written up on AMMS using template X noting observation, cause, effect and recommendation to facilitate inclusion in the audit report. Also supporting documentation (e.g. photocopies of supporting evidence should be retained).

4.133. Such documentation is necessary to ensure that all planned work has been properly carried out and that sufficient evidence has been obtained to support the audit conclusions and recommendations, and also to ensure that paragraphs in the audit report are fully supported.

Concluding by Audit Area

4.134. When each individual audit programme has been completed, a conclusion should be made for each audit area as to whether all planned work has been completed and whether more work is needed. Any further work to that planned should be agreed with the team leader. If no further audit work is considered necessary, then a conclusion should be made for each audit area as to whether the planned assurance has been obtained towards all relevant audit assertions. In cases where errors have been identified, they should be extrapolated where appropriate to evaluate whether they are material.

4.135. Also, for each audit area, audit findings of a similar nature should be grouped and summarised and included in a list of all proposed findings, with observation, cause, effect and recommendation for inclusion in the audit report.

Overall Conclusion

4.136. Conclusions for all audit areas should be brought together and summarised in order to evaluate the total extent of error in the audit and decide the appropriate overall opinion to give – see the next chapter for details. Further guidance on concluding is given at paragraph 5.6.

Quality Control Over Audit Fieldwork

4.137. All working papers and matrices of test results loaded on to AMMS by junior members of audit team should be reviewed by a senior member of audit team or team leader. The reviewer should ensure that the working paper or matrix of test results has been properly completed in order to evidence work done and that the appropriate test or tests has/have been signed off on the audit programme. For each audit programme test, the reviewer should ensure that there is a conclusion in terms of the extent to which the results of the test give assurance towards the planned audit assertions.

Follow-up of the Recommendations of Past Audits

4.138. In each audit, as part of routine fieldwork, the auditor should follow-up on the recommendations raised by previous audits where they have at that date seen no evidence that the recommendation was implemented. The follow-up work should document how the auditor has satisfied themselves that the recommendation has been implemented. If the recommendation has not been implemented or has only been partially implemented, then the recommendation should be once again raised in the audit report under a section entitled ‘Follow-up of past audit recommendations’ specifying the date the recommendation was made and repeating the recommendation and stating the circumstances/reasons for non-implementation. If the recommendation has become unnecessary then the auditor should formally write up in their audit findings why the recommendation should be dropped.

Chapter 5 Audit Reporting

Background

5.1. The purpose of this chapter is to consider the procedures necessary to draw together the results of the audit work and form an opinion on the financial statements (for financial audits) and on regularity (for both financial and compliance audits), including where the CAG qualifies or otherwise modifies his audit opinion. It provides guidance on the format of the auditor's report. It also sets out specific public sector aspects of reporting, including the regularity opinion and the CAG's reports to Parliament, as well as arrangements for the delegation of the CAG's responsibilities for signing the audit certificate.

Objectives

5.2. The objectives of the auditor are to:

a) design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity;

b) form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained;

c) express clearly that opinion through a written report that also describes the basis for the opinion;

d) express clearly an appropriately modified opinion on the financial statements that is necessary when:

- the auditor concludes, based on the audit evidence obtained, that the financial statements as a whole are not free from material misstatement; or
- the auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement; and

e) having formed an opinion on the financial statements, draw the users' attention, when in the auditor's judgement is necessary to do so, by way of clear additional communication in the auditor's report, to:

- a matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users' understanding of the financial statements; or
- as appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

5.3. In circumstances where the CAG is required under legislation to examine, certify and report, the objectives of the auditor extend to reporting on significant matters which should be brought to the attention of Parliament.

Relevant ISSAI and Other Guidance

5.4. The basic requirements which should be adhered to in respect of OCAG audits are contained in International Standards of Supreme Audit Institutions (ISSAIs) and International Standards on Auditing (ISAs). The main requirements and guidance which impact on this area of the audit are contained in ISSAI 1700 and ISA 700 "The Auditor's Report on Financial Statements", ISSAI 1705 and ISA 705 "Modifications to the Opinion in the Auditor's Report", and ISSAI 1706 and ISA 706 "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report".

5.5. All OCAG audits must comply with these standards. The guidance contained in this chapter emphasises the requirements of these standards and interprets the requirements in an OCAG context. Where relevant, the paragraphs cross-reference the application guidance in the ISSAIs or ISAs.

Core Policies and Guidance

Concluding on the Results of the Audit

5.6. In concluding on the results of the audit the auditor is required to perform certain procedures which allow them to form an audit opinion. These comprise:

a) evaluating the sufficiency and appropriateness of the audit evidence obtained (ISA 330);
b) performing analytical procedures at the concluding stage of the audit (ISA 520);
c) completing an overall review of financial statements;
d) reconsidering the risk arising from fraud (ISA 240);
e) considering any inconsistency in, or doubts over the reliability of evidence (ISA 500); and
f) reconsidering the independence and objectivity of the audit team (ISA 220).

Evaluating the Sufficiency and Appropriateness of Audit Evidence

5.7. Based on the audit procedures performed and the audit evidence obtained, the Auditor should evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate. (Ref: ISA 330 para A60-A61)

5.8. An audit of financial statements is a cumulative and iterative process. As the auditor performs the planned audit procedures, the audit evidence obtained may cause us to modify the nature, timing or extent of other planned audit procedures. Information may come to their attention that differs significantly from the information on which the risk assessment was based. For example:

- the extent of misstatements detected by performing substantive procedures may alter their judgement about the risk assessments and may indicate a significant deficiency in internal control;
- the auditor may become aware of discrepancies in accounting records, or conflicting or missing evidence; or
- concluding analytical procedures may indicate a previously unrecognised risk of material misstatement.

5.9. In such circumstances, the auditor may need to re-evaluate the planned audit procedures, based on the revised consideration of assessed risks for all or some of the classes of transactions, account balances, or disclosures and related assertions. ISA 315 contains further guidance on revising the risk assessment.

5.10. The auditor cannot assume that an instance of fraud or error is an isolated occurrence. Therefore, the consideration of how the detection of a misstatement affects the assessed risks of material misstatement is important in determining whether the assessment remains appropriate.

5.11. The auditor should conclude whether sufficient appropriate audit evidence has been obtained. In forming an opinion, the auditor should consider all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements. (Ref: ISA 330 para A62)

5.12. If the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion, they should attempt to obtain further audit evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, they shall express a qualified opinion or disclaim an opinion on the financial statements.

5.13. The auditor’s judgement as to what constitutes sufficient appropriate audit evidence is influenced by such factors as:

- the significance of the potential misstatement in the assertion and the likelihood of its having a material effect, individually or aggregated with other potential misstatements, on the financial statements;
- the effectiveness of management's responses and controls to address the risks;
- experience gained during previous audits with respect to similar potential misstatements;
- the results of audit procedures performed, including whether such audit procedures identified specific instances of fraud or error;
- the source and reliability of the available information;

- persuasiveness of the audit evidence; and
- understanding of the entity and its environment, including the entity's internal control.

5.14. The Team Leader or Director General should review and assess the audit evidence obtained during the course of the audit and conclude whether this provides a suitable basis for the audit opinion. This can be facilitated by on-going dialogue within the auditors working on the audit during the course of the audit and the use of on-site or 'hot' review.

Concluding Analytical Procedures

5.15. The auditor should design and perform analytical procedures near the end of the audit to assist in forming an overall conclusion as to whether the financial statements are consistent with the understanding of the entity. (Ref: ISA 520 para A17-19)

5.16. Concluding Analytical Procedures are intended to corroborate conclusions formed during the audit of individual components or elements of the financial statements. This enables the team to draw reasonable conclusions on which to base the audit opinion.

5.17. The analytical procedures performed may be similar to those used for Preliminary Analytical Procedures as a part of Risk Assessment Procedures, but will reflect the final financial statement position.

5.18. Considerations when carrying out such procedures may include:

a) whether the financial statements adequately reflect the information and explanations previously obtained and conclusions previously reached during the course of the audit;
b) whether the procedures reveal any new factors which may affect the presentation of or disclosures in the financial statements;
c) whether analytical procedures applied when completing the audit, such as comparing the information in the financial statements with other pertinent data, produce results which assist in arriving at the overall conclusion as to whether the financial statements as a whole are consistent with their knowledge of the entity's business;
d) whether the presentation adopted in the financial statements may have been unduly influenced by the desire of those charged with governance to present matters in a favourable or unfavourable light; and
e) the potential impact on the financial statements of the aggregate of uncorrected misstatements (including those arising from bias in making accounting estimates) identified during the course of the audit and the preceding period's audit, if any.

5.19. The results of such analytical procedures may identify a previously unrecognised risk of material misstatement. In such circumstances, ISSAI 1315 requires the auditor to revise their assessment of the risks of material misstatement and may require the performance of further controls and/or substantive procedures. This work should be documented on AMMS and carried out by the team leader.

Example: Issues identified in concluding analytical procedures
The entity has a target to make efficiency savings of 2% on prior period. In the draft account, efficiency savings of 2.5% had been made. A number of client and audit adjustments were identified that reduced the saving. In performing the concluding analytical procedures on the final account (i.e. after booked audit adjustments), the team calculated the actual savings that had been made, which were 2.01%. Unadjusted audit adjustments were equivalent to 0.02% of spend, and management had declined to adjust them on the grounds that they were not material. The auditor considered that the presentation adopted was unduly influenced by the desire of management to present matters in a favourable light, and that the unadjusted misstatements were qualitatively material.

Overall Review of the Financial Statements

5.20. Guidance on procedures to be performed in relation to the financial statements as a whole is set out in Chapter 4 of the manual, Section on Auditing the Financial Statements and Disclosures.

5.21. To the extent that they have not already done so in evaluation presentation and disclosures, and performing analytical procedures at the concluding stage of the audit, the Director General and Audit Manager should perform an overall review of the financial statements and document this review on AMMS. The purpose of this review is to determine whether:

- the financial statements have been prepared using the most appropriate accounting policies and that such policies have been consistently applied;
- the results shown in the financial statements are consistent with their knowledge of the business;
- all necessary disclosures are contained in the financial statements and are appropriately presented and clearly expressed; and
- the uncorrected misstatements and disclosure deficiencies are immaterial to the financial statements.

Consideration of Fraud Risk

5.22. ISA 240 'The Auditor's Responsibility Relating to Fraud in an Audit of Financial Statements' provides detailed guidance on their responsibility to consider fraud at all stages during the course of the audit.

5.23. The auditor should evaluate whether analytical procedures that are performed near the end of the audit, when forming an overall conclusion as to whether the financial statements are consistent with their understanding of the entity, indicate a previously unrecognised risk of material misstatement due to fraud (Ref: ISA 240 para A50). This evaluation should be documented on AMMS.

5.24. If the auditor identifies a misstatement, they should evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor should evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations, recognizing that an instance of fraud is unlikely to be an isolated occurrence. (Ref: ISA 240 para A51)

5.25. If the auditor identifies a misstatement, whether material or not, and they have reason to believe that it is or may be the result of fraud and that management (in particular, senior management) is involved, the auditor should re-evaluate the assessment of the risks of material misstatement due to fraud and its resulting impact on the nature, timing and extent of audit procedures to respond to the assessed risks. The auditor should also consider whether circumstances or conditions indicate possible collusion involving employees, management or third parties when reconsidering the reliability of evidence previously obtained. (Ref: ISA 240 para A52)

5.26. If the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud the auditor should evaluate the implications for the audit. (Ref: ISA 240 para A53)

5.27. If the auditor identifies the possible existence of fraud and consider that this fraud could have a material impact on the financial statements the auditor must undertake additional testing in order to confirm or dispel the suspicion of fraud. If the additional testing undertaken does not confirm or dispel their suspicions, the auditor should discuss the issue with the entity's management and consider whether the potential fraud has been properly considered or corrected in the financial statements. If senior management are involved in the fraudulent activity then to avoid the risk of tipping off, the auditor should consider whether a report should be made to the Audit Committee (if one exists), or if there is no Audit Committee to at least the next level of management above (as appropriate).

5.28. Where the auditor confirms that the financial statements are materially misstated as a result of fraud, or is unable to confirm otherwise, the General Director should consider the implications for the audit opinion, in particular the audit opinion on regularity (or overall conclusion on regularity for a Compliance audit). More detailed guidance on modifications to the audit opinion is provided later in this chapter.

Inconsistency in, or Doubts Over Reliability of, Audit Evidence

5.29. If (a) audit evidence obtained from one source is inconsistent with that obtained from another; or (b) the auditor has doubts over the reliability of information to be used as audit evidence then the auditor should determine what modifications or additions to audit procedures are necessary to resolve the matter, and should consider the effect of the matter, if any, on other aspects of the audit. (Ref: ISA 500 para A57)

5.30. Obtaining audit evidence from different sources or of a different nature may indicate that an individual item of audit evidence is not reliable, such as when audit evidence obtained from one source is inconsistent with that obtained from another. This may be the case when, for example, responses to inquiries of management, internal audit, and others are inconsistent, or when responses to inquiries of those charged with governance made to corroborate the responses to inquiries of management are inconsistent with the response by management.

5.31. Forming an opinion where there is conflicting audit evidence requires careful audit judgement. ISA 230 includes a specific documentation requirement if the auditor has identified information that is inconsistent with final conclusion regarding a significant matter, and the consideration of these issues, including any consultation, should be reflected within the documentation accordingly.

Evaluation of Independence and Ethical Issues

5.32. The Director General should consider the independence and objectivity of the audit team at the planning stage of the audit and document this consideration on AMMS.

5.33. In addition, the Director General must also consider any independence or ethical issues which arise during the audit and evaluate the impact of any identified breaches of the OCAG's policies and procedures to determine whether any such breaches represent a threat to the independence and objectivity of the CAG, and if any such cases are identified should detail consideration and relevant action on AMMS.

Forming an Audit Opinion

5.34. The auditor's report on the financial statements shall contain a clear written expression of opinion on the financial statements taken as a whole, based on their evaluation of the conclusions drawn from the audit evidence obtained, including evaluating whether:

a) sufficient appropriate audit evidence as to whether the financial statements as a whole are free from material misstatement;
b) obtain sufficient information as to whether the financial statement is free from fraud or error;
c) uncorrected misstatements are material, individually or in aggregate. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgements; (Ref: ISA 700 para A1-A3)
d) in respect of a true and fair framework, the financial statements, including the related notes, give a true and fair view; and
e) in respect of all frameworks the financial statements have been prepared in all material respects in accordance with the framework, including the requirements of applicable law.

5.35. In particular, the auditor should evaluate whether:

a) the financial statements adequately refer to or describe the relevant financial reporting framework;
b) the financial statements adequately disclose the significant accounting policies selected and applied;
c) the accounting policies selected and applied are consistent with the applicable financial reporting framework, and are appropriate in the circumstances;
d) accounting estimates are reasonable;
e) the information presented in the financial statements is relevant, reliable, comparable and understandable;
f) the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and
g) the terminologies used in the financial statements, including the title of each financial statement, is appropriate.

5.36. For audits where an audit opinion is given on regularity, the auditor's report shall also contain a clear written expression, based on the auditor evaluating the conclusions drawn from the audit evidence obtained, as to whether, in all material respects, the resources have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

5.37. In forming a judgement on the regularity opinion, and when concluding on compliance audits, the auditor should conclude on whether in all material respects, the transactions presented in the financial statements have been made in accordance with:

- authorising legislation;
- regulations issued under governing legislation;
- Parliamentary authorities; and
- Treasury authorities.

5.38. Examples of compliance deviations are given in Appendix 6.

5.39. Where the auditor identifies instances of irregularity materiality considerations apply. Their assessment of whether a failure to comply with any of the above is material to the financial statements will depend upon the monetary value of the irregularity, the circumstances in which it arose, the impact that it will have on the users of the account and the level of parliamentary and public interest in the issue. A minute from the Director General must be included on the audit file for all qualified audits.

5.40. The findings of the audit should be considered in the context of the materiality for the audit - not merely in terms of materiality by value, but also in terms of materiality by nature and by context. This consideration should be documented on AMMS. When evaluating audit differences, the audit team should consider:

- the significance to the readers of the account of the uncorrected difference to the financial statement either for individual line items or the financial statements as a whole;
- the likelihood that the undetected misstatements (when considered with uncorrected misstatements) may exceed materiality by value;
- the cause of the misstatement for example has it arisen as a result of fraudulent activity; and
- whether the identified misstatement may indicate a pattern of activity. In such circumstances the auditor must consider and document whether it is necessary to undertake additional audit procedures to identify whether other similar audit differences exist.

5.41. It is necessary to exercise a high degree of professional judgement in determining the audit opinion. This judgement should be properly documented on AMMS and reviewed/approved by team leader and Director General.

Types of Audit Opinion

5.42. ISSAI references:

- ISSAI 1700

“Forming an Opinion and Reporting on Financial Statements”

- ISSAI 1705

  “Modifications to the Opinion in the Independent Auditor’s Report”

5.43. The different types of ‘opinion’ are:

- Unqualified
- Qualified
- Adverse
- Disclaimer

5.44. Example of an unqualified audit opinion:

- Council of xxx
- An accruals IPSAS account
- Present fairly opinion
- Regularity paragraph
- Long form report on compliance audit work

5.45. Example of a qualified audit opinion:

- xxx- financial statements of xxx Revenue and Customs
- Qualification of regularity opinion for tax credits
- Financial statements get a true and fair opinion apart from this
- Note the opinion on other matters
- A separate report is referred to giving more details

5.46. Example of an adverse audit opinion:

- xxx -Commission’s Client Funds Account
- Adverse opinion on Note xxx “Outstanding Maintenance Arrears” which does not give a true and fair view of the outstanding maintenance balances as at xx June 20xx
- Report giving further details

5.47. Example of a disclaimer audit opinion:

- xxx Government 20xx
- Certain material weaknesses in internal control over financial reporting and other limitations on the scope of the work resulted in conditions that prevented the auditors from expressing an opinion on the fiscal years 20xx and 20xx accrual-based consolidated financial statements.
- Tests of compliance with selected provisions of laws and regulations for fiscal year 20xx were limited by the material weaknesses and other scope limitations discussed in the report.

The Auditor's Report

5.48. It is important that the form and content of audit certificates and audit reports are presented in a uniform fashion, as this promotes the reader's understanding of the certificate/report, and highlights unusual circumstances when they occur. The auditor's certificate/report will therefore include the following elements:

- Title;
- Addressee;
- Introductory paragraph identifying the statements to be audited;
- Respective responsibilities of those charged with governance and the auditor;
- Scope of the audit of the financial statements
- Opinion on the financial statements
- Opinion in respect of an additional financial reporting framework;
- Opinion on Other Matters
- Details of audit observations (should be included and discussion on this point should be included between 5.74 and 5.75)
- Date of the report;
- Auditor's address; and
- Auditor's signature.

5.49. These elements, as appropriate, are considered in more detail below.

Title

5.50. The auditor's report shall have an appropriate title. (Ref: ISA 700 para A4)

5.51. The title used for the auditor's report should adopt the wording used in the legislation appointing the CAG as auditor. Where there is a statutory requirement for his examination to be certified, an audit report containing the opinion of the CAG on financial statements is entitled 'Audit Certificate'. Use of the word 'certificate' clearly differentiates the audit report from any other report of the CAG. Where the CAG undertakes the audit by statutory appointment, the terms of the statute may require him to examine, certify and report on the financial statements. Where a separate substantive report is not required the report will be included within the body of the audit certificate. In such cases, the document will be entitled the 'Certificate and Report of the Comptroller and Auditor General'.

5.52. Where the CAG is the appointed auditor in legislation, but there is no statutory requirement to 'certify', the title of the audit report should be "Audit report of the Comptroller and Auditor General to [addressee of audit report]."

5.53. For audits performed by agreement, the title used for the auditor's report should be the "Independent Auditor's Report".

Addressee

5.54. The auditor's report should be appropriately addressed as required by the circumstances of the engagement. (Ref: ISA 700 para A5).

5.55. The certificate should be appropriately addressed as required by the circumstances of the engagement and any local regulations. The addressee would normally be the person on whose behalf the audit was undertaken. For government entities, the audit is usually undertaken on behalf of Parliament (as dictated by governing legislation). The legislation appointing the CAG should be consulted to determine the appropriate addressee(s), based on where the financial statements will be laid. The exceptions to this are where:

- legislation requires the appointment of the auditor and specifies the person or persons to whom the auditor shall report; or
- the audited financial statements are not required to be laid before Parliament. In such cases it is necessary to consider on whose behalf the audit is being undertaken. Although this is normally the person, or persons, making the appointment, the auditor may need to look behind this.

Introductory Paragraph

5.56. The auditor's report should identify the financial statements of the entity that have been audited, including the date of, and period covered by, the financial statements. Where the financial statements being audited are those of a company, this section should specify that the financial reporting framework that has been applied in their preparation is applicable law and Bangladesh Financial Reporting Standards (BFRS)/IFRS.

Respective Responsibilities of Those Charged with Governance and the Auditor

5.57. The auditor's report should include a statement that those charged with governance are responsible for the preparation of the financial statements and a statement that the responsibility of the auditor is to audit and express an opinion on the financial statements in accordance with applicable legal requirements and International Standards on Auditing. The report shall also state that those standards require the auditor to comply with Ethical Standards for Auditors. (Ref: ISA 700 para A6 - A7)

5.58. Where there is a statutory requirement for the CAG to "examine, certify and report", the responsibility of the CAG in this paragraph of the certificate will be described as "audit, certify and report on the financial statements". Otherwise the description of the CAG's responsibilities will be "audit and express an opinion on the financial statements".

5.59. Where the CAG is appointed by legislation to audit an entity which is not a company, the applicable legal requirements are contained in the appointing legislation. Therefore, the responsibility of the CAG will be described as being in accordance with the relevant Act, rather than "applicable legal requirements and International Standards on Auditing".

Where there is no statutory basis for the audit, the equivalent sentence will end after "on the financial statements".

5.60. For non-company audits, the CAG chooses to audit in accordance with International Standards on Auditing, so this section will state that "I have conducted my audit in accordance with International Standards on Auditing".

Scope of the Audit of the Financial Statements

5.61. The auditor's report should include the following description of the scope of an audit:

"An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the *[describe nature of entity]* circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by responsible persons of the audited entity *[describe those charged with governance]*; and the overall presentation of the financial statements". (Ref: ISA 700 para A8 – A9)

5.62. The scope section of the audit report/certificate should also identify the other information that has been read by the auditor (in accordance with ISA 720A and ISA 720B) to identify material inconsistencies with the financial statements. This should describe all the information the auditor expects to be published in the same document as the financial statements and the audit report. Where the term 'annual report' is not an accurate description of this information, the titles of the individual sections will need to be specified.

5.63. Where a regularity opinion is provided, the following paragraph will be included within the description of the scope of an audit:

"In addition, I am required to obtain evidence sufficient to give reasonable assurance that the [income and expenditure/receipts and payments] reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them."

Opinion on the Financial Statements

5.64. The opinion paragraph of the auditor's report should clearly state the auditor's opinion as required by the relevant financial reporting framework used to prepare the financial statements, including applicable law.

5.65. When expressing an unqualified opinion on financial statements prepared in accordance with a true and fair framework the opinion paragraph shall clearly state that the financial statements give a true and fair view.

5.66. It is not sufficient for the auditor to conclude that the financial statements give a true and fair view solely on the basis that the financial statements were prepared in accordance with accounting standards and any other applicable legal requirements, as additional disclosures or explanations may be required to give a true and fair view. (Ref: ISA 700 para A10 – A12)

5.67. In public sector, these requirements are usually set out in an accounts direction issued by Treasury, and the further primary statements required by accounting standards, the auditor must refer to all such statements when expressing the audit opinion.

5.68. Public sector financial statements may include an opinion as to whether the financial statements give a true and fair view, or the auditing framework may require an opinion as to whether the financial statements present fairly or properly present the entity's transactions or balances. Whichever wording is used for the opinion on the financial statements, this will not have an impact on the extent to which the auditor observes the requirements of Auditing Standards.

Opinion in Respect of an Additional Financial Reporting Framework

5.69. When the auditor is engaged to issue an opinion on the compliance of the financial statements with an additional financial reporting framework the second opinion should be clearly separated from the first opinion on the financial statements, by use of an appropriate heading. (Ref: ISA 700 para A13)

Opinion on Other Matters

5.70. When the auditor also addresses other reporting responsibilities within the auditor's report on the financial statements, the opinion arising from such other responsibilities should be set out in a separate section of the auditor's report following the opinion(s) on the financial statements or, where there is one, the opinion on regularity. (Ref: ISA 700 para A15 – A16)

5.71. If the auditor is required to report on certain matters by exception they should describe the C&AG's responsibilities under the heading "Matters on which they are required to report by exception" and incorporate a suitable conclusion in respect of such matters. (Ref: ISA 700 para A17 - A18)

5.72. The auditor reports by exception on whether:

- adequate accounting records have not been kept [or returns adequate for their audit have not been received from branches not visited by their staff]; and
- the financial statements are not in agreement with the accounting records or returns; and

- all of the information and explanations required for the audit have not been received.

5.73. For all audits on which the auditor qualifies their opinion on the basis of a limitation of scope, they should also consider whether they need to state that proper accounting records have not been kept.

> ***Example: Details of Audit Observations***
>
> For each audit observation, there should firstly be a numbered title to the point in bold font starting at 1, and size of the error should be included in the title. Below the title brief details of the observation should be given with supporting data or reference with detailed supporting Annexure. Below this point there should be a Cause section which should detail the weakness or failure in internal control that allowed the observation to happen. Below that is the effect section which should state if the point or error is material and quantification should be given where possible (to agree with the value in the title). Below that is the Recommendation section which will generally link to the effect section and suggest the new or improved internal control that is needed to prevent a recurrence of the point or error. Lastly there should be a section for management response which should be left blank until the draft audit recommendation is sent to management for comment/response, when they should be encouraged to say if the recommendation is accepted and if so who will be responsible for implementing it and by when.
>
> It is acceptable but not essential to have an interim management response for findings raised with management at the time of the fieldwork, but space should always be left below for the response to be confirmed in the formal clearance stage for the report.

Date of the Certificate

5.74. The date of an auditor's report on a reporting entity's financial statements should be the date on which the CAG (or a delegate) signed the report expressing an opinion on those financial statements. (Ref. ISA 700 para A19)

5.75. The auditor should not sign, and hence date, the report earlier than the date on which all other information contained in a report of which the audited financial statements form a part have been approved by those charged with governance and the auditor has considered all necessary available evidence. (Ref. ISA 700 para A20 – A23)

5.76. If the certificate is signed at a date later than that on which the Accounting Officer approved the financial statements, the Director General should obtain assurance that the Accounting Officer would have approved the financial statements at the certification date and ensure that the review of post balance sheet events covers the period up to the date of signature. Such assurance must be obtained from or directly on behalf of the Accounting Officer.

Auditor's Address

5.77. The report should name the location of the office where the auditor is based.

Auditor's Signature

5.78. The auditor's report should state the name of the auditor and be signed and dated. (Ref. ISA 700 para A24)

5.79. For audits carried out by the OCAG, the audit certificate is signed by the CAG. Where responsibility for signing the certificate is delegated by the CAG to the Director General, the Director General should sign personally, with the words "for and on behalf of the Comptroller and Auditor General" appearing below their name.

5.80. If the audit team fails to obtain all the information and explanations which, to the best of their knowledge and belief, are necessary for the purposes of their audit, the CAG will state this fact on his certificate. For all audits on which the auditors qualify their opinion on the basis of a limitation of scope, the auditor should also consider whether they need to state that proper accounting records have not been kept.

Modification to the Opinion in the Auditor's Report (ISA 705)

5.81. The auditor should modify the opinion in the auditor's report when:

a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; (Ref: ISA 705 para A2-A7) or

b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. (Ref: ISA 705 para A8-A12)

5.82. ISA 700 establishes three types of modified opinions:

- Qualified opinion;
- Disclaimer opinion;
- Adverse opinion.

5.83. The auditor's judgement of the nature of the matter giving rise to the opinion and the pervasiveness of its effects on the financial statements affects the type of the opinion to be expressed:

Nature of Matter Giving Rise to the Modification	Auditor's Judgement about the pervasiveness of the Effects or Possible Effects on the Financial Statement	
Financial statements are materially misstated	Qualified opinion-except for disagreement	Adverse opinion
Inability to obtain sufficient appropriates audit evidence	Qualified opinion- except for limitation of scope	Disclaimer of opinion

5.84. To ensure that modified certificates are clear and easy to understand, it is important to maintain as much uniformity as possible in the content and style of the certificates. Accordingly suggested wording has been given in ISA 705.

5.85. A flowchart outlining the steps to consider when forming an opinion on the financial statements is set out in the Appendix 1 to this chapter.

Qualified Opinion

5.86. The auditor should issue a qualified opinion when:

a) Having obtained sufficient appropriate audit evidence, they conclude that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or

b) They are unable to obtain sufficient appropriate audit evidence on which to base the opinion, but they conclude that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive. (Limitation of scope)

5.87. Where a regularity opinion is provided as part of the audit engagement, they should issue a qualified opinion on regularity when:

a) Having obtained sufficient appropriate audit evidence, the auditor concludes that irregularities, individually or in the aggregate, are material to the financial statements; or

b) They are unable to obtain sufficient appropriate audit evidence on which to base the regularity opinion.

5.88. A material misstatement of the financial statements may arise in relation to:

- the appropriateness of the selected accounting policies;
- the application of the selected accounting policies; or
- the appropriateness or adequacy of disclosures in the financial statements.

5.89. A limitation of scope may arise from:

- circumstances beyond the control of the entity;
- circumstances relating to the nature and timing of the auditor's work; or
- limitations imposed by management.

Limitations of Scope

5.90. Where a limitation is imposed by the entity prior to the acceptance of an audit engagement, the auditor should consider whether it is appropriate to accept the engagement. If a limitation is imposed by the entity after accepting the audit engagement, and the entity will not remove the limitation, they should consider if it is appropriate to resign from the engagement. In the public sector, where they are appointed under statute, it is not possible to decline or withdraw from the engagement. In these circumstances, the CAG has the statutory authority to report such matters to Parliament.

5.91. If, after accepting the engagement, they become aware that management has imposed a limitation on the scope of the audit that they consider likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, they should request that management remove the limitation.

5.92. If management refuses to remove the limitation, they should communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity, and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.

5.93. If the auditor is unable to obtain sufficient appropriate audit evidence, they should determine the implications as follows:

- if the auditor conclude that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor should qualify the opinion; or
- if the auditor conclude that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, they should:
    - ➢ withdraw from the audit, where practicable and possible under applicable law or regulation; (Ref: ISA 705 Para A13-A14)
    - ➢ if withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

5.94. Where the auditor is appointed under statute, it is not possible to decline or withdraw from the engagement. In these circumstances, the CAG has the statutory authority to report such matters to Parliament.

5.95. If the auditor is able to withdraw from an engagement, and determine they should do so, before withdrawing they should communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion. (Ref: ISA 705 para A15)

Adverse Opinion

5.96. The auditor should express an adverse opinion when, having obtained sufficient appropriate audit evidence, they conclude that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

5.97. The term *pervasive* is **defined** in the ISA:

Pervasive – A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence. Pervasive effects on the financial statements are those that, in the auditor's judgement:

(i) Are not confined to specific elements, accounts or items of the financial statements;

(ii) If so confined, represent or could represent a substantial proportion of the financial statements; or

(iii) In relation to disclosures, are fundamental to users' understanding of the financial statements.

5.98. Reporting objectives for financial statements in the public sector, and the sensitivity of users to misstatement, are not generally linked to single figure such as profit / loss or net assets to the same extent as for private sector entities. Consequently, it is rarer that a misstatement would be deemed to be pervasive to the financial statements as a whole.

Disclaimer Opinion

5.99. The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and they conclude that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

5.100. The auditor should disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, they conclude that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

5.101. Reporting objectives for financial statements in the public sector, and the sensitivity of users to misstatement, are not generally linked to single figure such as profit / loss or net assets to the same extent as for private sector entities. Consequently, it is rarer that a limitation in scope would be deemed to be pervasive to the financial statements as a whole, and it would be more common to issue an opinion containing multiple limitations in scope.

Impact of a Prior Year Qualification

5.102. If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which give rise to the modification is unresolved, they should modify the auditor's opinion on the current period's financial statements.

5.103. In the basis for modification paragraph in the auditor's report, they should either:

a) refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or

b) in other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures. (Ref: ISA 710 para A3-A5)

5.104. If the matter that gave rise to the modified opinion has been resolved and properly corrected in the prior year comparatives in the financial statements, the current certificate does not need to refer to the previous modification. However, if the matter is material to the current period, the auditor may want to include an emphasis of matter paragraph to give further information about the situation.

Opinion on Other Information Presented with the Accounts

5.105. The auditor's responsibilities extend to the other information disclosed in the annual report and accounts, which they are not required to audit, but for which they are required to consider the consistency with the accounts and with their knowledge of the business.

Negative Consistency Opinion

5.106 ISA 720A requires the auditor to consider the consistency of all information reported alongside the audited financial statements, including the Statement on Internal Control.

5.107. The auditor should read the other information to identify material inconsistencies, if any, with the audited financial statements. (Ref: ISA 720 para A4-1 – A4-2)

5.108. If, on reading the other information, the auditor identifies a material inconsistency, they shall determine whether the audited financial statements or the other information needs to be revised.

5.109. If revision of the audited financial statements is necessary and management refuses to make the revision, they should modify the opinion in the auditor's report in accordance with ISA 705.

5.110. If revision of the other information is necessary and management refuses to make the revision, the auditor should communicate this matter to those charged with governance, unless all of those charged with governance are involved in managing the entity; and

a) include in the auditor's report an Other Matter(s) paragraph describing the material inconsistency in accordance with ISA 706; or
b) withhold the auditor's report; or
c) withdraw from the engagements where withdrawal is possible under applicable law or regulation. (Ref: ISA 720 para A6-A7, para A11-2 – A11-3)

Impact on Audit Opinion

5.111. Where the other information is consistent with the audited financial statements, no further information is required by the auditor.

5.112. If, on reading the other information, the auditor identifies a material inconsistency or misstatement, they should determine whether the audited financial statements or the other information need to be amended.

5.113. Where material inconsistencies or misstatements are identified, they should try to resolve them by discussions with those charged with governance. Where these issues cannot be resolved through discussion, it may be appropriate for the auditor to consider requesting those charged with governance to consult with a suitably qualified third party, such as the entity's lawyers, to obtain further advice.

5.114. If the auditor is still of the opinion that an amendment is required to either the audited financial statements or the other information, but none is made, they should consider appropriate action, including the implications for the audit opinion as follows:

- if amendments are necessary to the audited financial statements and the entity refuses to make such amendments, they should express a qualified or adverse opinion.
- if amendments are necessary to the other information and the entity refuses to make such amendments, they should include an 'Other Matter' paragraph in the audit certificate explaining the details of the material inconsistency. This does not give rise to a qualified opinion in circumstances where there is no impact on the truth and fairness of the financial statements.

5.115. The auditor should consider the nature and severity of the inconsistency or misstatement that exists, and a distinction should be drawn between those issues that are a matter of fact and those issues that are a matter of judgement. It is far more difficult to disagree with a matter of judgement (such as a view on the likely outturn for the following year) than a factual error.

5.116. There may be circumstances in which the auditor is aware that the expressed view of those charged with governance is significantly at variance with the entity's internal assessment of an issue, or is so unreasonable as not to be credible to someone with the auditor's knowledge. When determining what action should be taken, the auditor may need to take legal advice, including advice on whether the auditor would be protected by qualified privilege from a defamation claim if they were to refer to the matters in their report or subsequently.

Emphasis of Matter and Other Matter Paragraphs

5.117. In some circumstances it may be necessary, without modifying the audit opinion, to draw the users' attention to a matter, disclosed or not disclosed in the financial statements, that is relevant to the users' understanding of the financial statements. This may take the form of an Emphasis of Matter paragraph, or an Other Matter paragraph. These are defined in ISA 706 as follows:

- Emphasis of Matter paragraph – A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements.
- Other Matter paragraph – A paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

5.118. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor should include an Emphasis of Matter paragraph in the auditor's report provided the auditor has obtained sufficient appropriate audit evidence that the matter is not materially misstated in the financial statements. Such a paragraph shall refer only to information presented or disclosed in the financial statements. (Ref: ISA 706 para A1-A2)

5.119. An emphasis of matter paragraph would be included in the audit certificate directly after the opinion paragraph to which it relates, and would refer to the fact that the auditor's opinion is not qualified in respect of the matter.

5.120. The use of an emphasis of matter paragraph should not be routine as this diminishes the effectiveness of the communication of such matters. In addition, it should not be used to compensate for inadequate disclosure by the reporting body – the absence of disclosures required to provide a true and fair view would lead to a qualified opinion. We consider emphasis of matter paragraphs under four circumstances:

- there is a material uncertainty relating to the going concern assumption;
- the accounts are prepared on a basis other than going concern;
- there is a significant uncertainty relating to a future action or event which is outside the reporting entity's control and which, potentially, has a material impact on the financial statements;
- where the prior year accounts were qualified and the matter giving rise to the qualification has been resolved with appropriate disclosures or adjustments made to the corresponding figures, but the prior period financial statements have not been adjusted.

5.121. Uncertainties are regarded as significant when they involve a significant level of concern about matters whose potential effect on the financial statements is unusually great, or about the validity of the going concern basis. However, the opinion will be unqualified where the auditor considers that appropriate estimates and disclosures have been included in the financial statements. A common example of a significant uncertainty is the outcome of ongoing major litigation.

5.122. Uncertainty contained within an accounting estimate, such as an actuarial valuation, will not necessarily give rise to an emphasis of matter. Uncertainties inherent in accounting estimates should be considered in accordance with ISA 540: Auditing Accounting Estimates, including Fair Value Accounting Estimates and Related Disclosures. Where the auditor considers that the accounting estimate is reasonable in the circumstances, an emphasis of matter paragraph would not routinely be included in the certificate.

5.123. The emphasis of matter paragraph should give details of the matter giving rise to the significant uncertainty, and its possible effects on the financial statements, including quantification if possible. Where it is not possible to quantify the effects on the financial statements, a statement to this effect should be included. Clarity for the reader is enhanced by using an appropriate sub-heading in the report to differentiate the emphasis of matter paragraph from other paragraphs in the audit certificate.

5.124. In determining whether an uncertainty is significant, the Engagement Team should consider:

- the risk that an estimate included in financial statements may be subject to change;
- the range of possible outcomes; and
- the consequences of those outcomes on the view shown in the financial statements.

5.125. An emphasis of matter paragraph may also be used to report on other matters that affect the financial statements. An example of this is where an amendment is required to the other information published with the audited financial statements and the entity refuse to make the amendment – the auditor would consider referring to this in an emphasis of matter paragraph.

5.126. If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in their judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report and this is not prohibited by law or regulation, they should do so in a paragraph in the auditor's report, with the heading "Other Matter," or other appropriate heading.

5.127. The following are examples of where it may be appropriate to include an Other Matter paragraph:

- where the auditor is unable to withdraw from an engagement even though the possible effect of an inability to obtain sufficient appropriate audit evidence due to a limitation on the scope of the audit imposed by management is pervasive, the auditor may consider it necessary to include an Other Matter paragraph in the auditor's report to explain why it is not possible for us to withdraw from the engagement.
- where there is a material inconsistency between the financial statements and the surrounding information arising from a misstatement in the surrounding information; or
- where financial statements are prepared for a specific purpose in accordance with a general purpose framework, because the intended users have determined that such general purpose financial statements meet their financial information needs, since the auditor's report is intended for specific users, they may consider it necessary in the circumstances to include an Other Matter paragraph, stating that the auditor's report is intended solely for the intended users, and should not be distributed to or used by other parties.

CAG's Reports

5.128. The CAG has wide ranging powers to report to Parliament. Such powers to report should be used to draw to the attention of Parliament matters which are necessary for the understanding of the financial statements or the entity's stewardship of public funds. It may also be used where there are other significant matters associated with the financial statements which he believes should be brought to Parliament's attention, even in circumstances where his opinion has not been qualified.

Reports on Qualified Financial Statements

5.129. Where the opinion on the financial statements is qualified, a CAG's Report will normally be presented. A separate report will always be required where:

- a limitation of scope is so pervasive as to necessitate a disclaimer of opinion;
- a disagreement is so fundamental as to lead to an adverse opinion; or
- the qualification is in respect of another material irregularity.

5.130. The first two circumstances above suggest either a fundamental breakdown in control or disagreement on a matter which could render the financial statements totally misleading. In either case Parliament would expect a detailed explanation beyond that which could be given in the certificate and which could form the basis of a hearing by the Committee of Public Accounts.

5.131. In the final circumstance outlined there have been a breach of Parliamentary control and Parliament will wish to be informed as to the nature of the breach, the reasons for this and the action taken by the entity to prevent such re-occurrence. The principles underlying the irregularity may also have a wider impact on public sector.

5.132. Where the CAG issues a qualified opinion for reasons other than those stated above, the Director General will make recommendations to the CAG on whether a separate report is necessary or not.

Reports on Unqualified Financial Statements

5.133. The CAG may also issue reports with financial statements when the opinion is not qualified. The Director General will be concerned with matters which have arisen during the course of the audit which although not material to the opinion are of sufficient importance to draw to the attention of Parliament.

5.134. These will normally fall into one of three categories:

- **Improprieties** - although propriety is not expressly covered in the audit opinion Parliament has clear expectations as to the way in which public business should be conducted. Significant improprieties which could be covered in a separate report might include matters such as a failure to make a proper distinction between private and public business, failure to demonstrate fair competition in the appointment of staff or the letting of contracts, and extravagant hospitality or expenses.
- **Inadequate financial control** - the CAG is not required to give an opinion on financial control but would be expected to draw to the attention of Parliament control weaknesses which placed public funds at significant risk either through fraud or error.

- **Other matters of interest** - the CAG may identify other matters which may be of interest to the addressee of the auditor's opinion arising from their audit.

Report Content

5.135. Each CAG's report will need to be tailored to the circumstances of each case, and so a standard pro-forma is not given. Nevertheless each report should make clear:

- the scope of the examination that has led to the report;
- why the CAG has considered it necessary to report;
- the precise nature of the irregularity, propriety or control weakness reported on;
- management's response to the issue and action taken or planned to prevent a reoccurrence;
- whether or not the opinion on the financial statements has been qualified in respect of the matter reported on; and
- whether the matter will have any future effect on the accounts.

Principal Accounting Officer's Clearance

5.136. All audit reports should be approved by the CAG. Before that it should be cleared by the Director General from the concerned the Principal Accounting Officer of the entity the auditor is reporting on. This will ensure that:

- all material and relevant facts have been included;
- the facts are not in dispute;
- the presentation and conclusions drawn from the facts are fair;
- the report distinguishes clearly between the facts and the conclusions drawn from them; and
- any disagreement with the conclusions on the part of the Accounting Officer are properly presented.

5.137. Draft reports that refer to third parties should be cleared at an appropriate level with the organisation or person concerned.

5.138. When the CAG will issue a report with the financial statements, the auditor should allow sufficient time within certification schedule.

Appendices

Appendix 1- Examples of Subject Matters, Subject Matter Information and Criteria in Compliance Auditing

The follow table is intended to give examples of subject matters, subject matter information and relevant criteria. The list is not intended to be an exhaustive overview. The particular subject matter, subject matter information and criteria will vary depending on a variety of matters such as the mandate of the SAI and the objective of the particular audit.

Sl. No.	Subject matter	Subject matter information	Criteria
1	Financial performance and use of appropriated funds. This may involve budget execution, including testing that funds have been used in accordance with the purposes and intentions as decided by the legislature. In many SAIs this type of compliance audit may be related to regularity audit, including the audit of financial statements. *More specific guidance on this particular topic is included in ISSAI 4200 - Appendix 1-A.*	Financial information such as financial statements	• Relevant budget legislation such as an appropriations act • Approved budget
2	Financial performance, for example revenues in the form of: • project funds from donor agencies • funds from governments • other similar types of funds and how they have been used	Project financial information / project accounts	• Relevant legislation relating to use of government funds (eg a 'single audit act') • The mandated activities of the audited entity • The terms of the funding Agreement

Sl. No.	Subject matter	Subject matter information	Criteria
3	Financial performance, for example revenues in the form of grants, and how the revenues have been used	Financial information related to the use of the grant	• The mandated activities of the audited entity • The terms of the grant agreement
4	Financial performance, for example revenues or expenditures in accordance with a contract or loan agreement, and how they have been used	Financial information related to the contract or loan agreement	The terms of the contract or loan agreement
5	Procurement	Financial information	• Relevant procurement legislation and regulations (national and international) • The terms of a contract with a supplier
6	Expenditures	• Financial information • Statement of compliance	• Relevant budget legislation such as an appropriations act • Other relevant legislation • Relevant ministerial directives, government policy requirements and resolutions of the legislature • The terms of a contract
7	Program activities	Activity indicators or reports	Relevant agreed levels of performance such as those set out in laws and regulations, ministerial directives, goals agreed by the legislature or the entity, international treaties, protocols, conventions or agreements, a service level agreement, the terms of a contract, generally established industry

Sl. No.	Subject matter	Subject matter information	Criteria
			standards, or reasonable public expectations. For example: • number of kindergarten places related to number of eligible children • number of qualified nurses and doctors per number of citizens • number of miles of road paved • number of months required to process benefit payments or building permits • frequency and quality of accounting information to be provided by a service organisation • number of building inspections to be performed within a particular time period • measures of results related to water quality, etc.
8	Service delivery	• A statement of service delivery • Publicly reported information	Relevant legislation or directives
9	Probity of a public administrative decision	• Citizen complaints register • Publicly reported information	Relevant legislation or directives
10	Corporate Social Responsibility (CSR), for example the audit of publicly funded projects in developing countries	A statement of compliance with CSR (or lack thereof)	Relevant legislation or directives in areas such as human and civil rights, gender equality, workplace, environment, etc.
11	Behaviour / Propriety	• A statement of compliance, for example a statement of independence (legal competence).	• Relevant legislation or directives covering behaviour of public sector officials.

Sl. No.	Subject matter	Subject matter information	Criteria
		• In the public sector this 'statement' may sometimes be implicit and related to the concepts of probity and propriety (see section on criteria above).	• A code of ethics or internally developed code of conduct • Stated values or leadership principles • Internal policies, manuals and guidelines • The terms of reference of the organisation, the bylaws or similar • The terms of a contract (e.g. agreed confidentiality or quarantine arrangements subsequent to certain employment situations)
12	Membership obligations	A statement of compliance	Agreed terms of membership
13	Processes related to health and safety	• A statement of compliance • Financial transactions	• Relevant occupational health and safety legislation, for example, related to handicap access • Policies, processes, manuals, guidelines etc
14	Processes related to environmental protection	• A statement of compliance • Financial transactions	• Relevant environmental legislation, for example, related to water quality, waste disposal or carbon emissions levels • The terms of international environmental treaties, protocols, conventions or agreements • Policies, processes, manuals, guidelines etc
15	Internal control processes	• A statement of compliance	• An internal control

Sl. No.	Subject matter	Subject matter information	Criteria
		• Financial transactions	framework, for example COSO[2], CoCo or similar, or internal control requirements set out in relevant legislation or generally accepted within a jurisdiction • Policies, processes, manuals, guidelines etc
16	Processes particular to the entity's activities and operations, such as payment of pensions or social benefits, processing passport or citizenship applications, assessing fines or other forms of penal sentences	• A statement of compliance • Financial transactions	• Relevant legislation or directives • Policies, processes, manuals, guidelines etc
17	Physical characteristics	A specifications document or the physical object itself	• A building code (size, height, purpose, density measures for a particular zoned area, etc) • The terms of a construction contract, or other type of contract
18	Tax revenues, taxpayer obligations or other obligations involving reporting to regulatory authorities	• Individual or corporate tax returns • Other tax forms submitted to regulatory authorities (such as VAT forms, reporting forms for agencies operating within regulated industries such as banking and finance, pharmaceuticals, etc)	• Relevant legislation or industry specific codes • A tax code, revenue code or similar

[2] COSO – Committee of Sponsoring Organisations of the Treadway Commission. CoCo = Criteria of Control Board, The Canadian Institute of Chartered Accountants.

Appendix 2 – Examples of Sources to be used in Gaining an Understanding of the Audited Entity and Identifying Suitable Criteria

The following is an illustrative, but not exhaustive list of sources that public sector auditors may use in identifying suitable audit criteria:

a) Laws and regulations, including the documented intentions and premises for establishing such legislation
b) Budgetary legislation / approved budget or appropriations
c) Documents of the legislature related to budgetary laws or resolutions, and to the premises or particular provisions for use of approved appropriations, or for financial transactions, funds and balances
d) Legislative or ministerial directives
e) Information from regulatory authorities
f) Official records of meetings of the legislature, public accounts committee or similar committee of the legislature, or other public bodies
g) Principles of law
h) Legal precedent
i) Codes of practice or codes of conduct
j) Internal descriptions of policies, strategic and operational plans and procedures
k) Manuals or written guidelines
l) Formal agreements, such as contracts
m) Loan or grant agreements
n) Industry standards
o) Well established theory (for example theory for which there is general consensus. Such theory may be obtained, for example, from published information such as technical literature and methods, professional journals, etc, or through inquiry with knowledgeable sources such as experts in a particular field)
p) Generally accepted standards for a particular area (such standards are normally clearly identifiable standards that have their source in some form of legislation and that are a result of established practice and legal precedent, for example 'generally accepted accounting principles' in a particular country)
q) For audits of propriety: Principles for sound public sector financial management and conduct of public sector officials. Principles of conduct may arise from the

legislature's or public expectations regarding the behaviour of public sector officials. In some cases, these principles may be documented in only fragmentary ways. They may, in some cases, only be defined as a result of their breach.

Additional sources which public sector auditors may use to obtain an understanding about the audited entity, its environment and relevant program areas may include:

a) The entity's annual report

b) Legislative propositions and speeches

c) Websites

d) Published reports, articles in newspapers or journals, other media sources, etc

e) Knowledge obtained from previous audits

f) Information gathered through meetings and other communication

g) Minutes of Board or other management meetings

h) Internal audit reports

i) Official statistics

Appendix 3– Examples of Factors Related to Assessing Risk in Compliance Auditing

The following are examples of factors that may be considered in assessing risk in a compliance audit. The list is not intended to be exhaustive, and the factors will depend on the particular audit circumstances.

The Audited Entity's Objective and Mandate

1. Are the audited entity's objective, mandate and legal capacity clearly stated and readily available?
2. Have there been recent changes in mandate, objectives or program areas?
3. Are program areas or relevant subject matters clearly identifiable?
4. Do program areas overlap considerably with other entities such that there is a risk of duplication or of fragmentation?

Organisational Structure

1. What is the legal basis of the entity (ministry, directorate, agency etc) and from where does it derive its authority?
2. Does the audited entity have clearly defined roles and responsibilities, and related authority attaching to these?
3. Are these roles, responsibilities and authorities clearly communicated and understood throughout the entity?
4. If the entity is part of a hierarchic structure, and another entity is responsible for supervision of the audited entity, how does such supervision take place?
5. Does the organisation focus on risk assessment and risk management, including risks of non-compliance, in its operations?
6. Have there been recent organisational changes?
7. Are any activities outsourced to other entities?
8. If activities are outsourced, how is compliance and performance monitored?
9. Are there other potential risks associated with outsourcing?
10. Do personnel have adequate competence and ethical behaviour?
11. Do personnel seek relevant information and is relevant information easily accessible?
12. Is information communicated on a timely basis in the organisation?
13. Are there any aspects of organisational structure that could give rise to greater risk of fraud?

Political Considerations

1. To which level of government does the particular entity belong and does it have relations to other levels of government?

2. What are the responsibilities (constitutional or other) of the relevant minister, or of entity management?
3. What is experience in dealing with the entity's political vs. administrative management?
4. Is there political consensus, or are differing views freely expressed?
5. How is the political management comprised?
6. What are program areas of political focus, visibility and sensitivity?
7. How does the working relationship between political and administrative management function?
8. Are there any areas of particular public interest?
9. What is experience in relation to one entity exercising unfavourable influence on other related entities in the public sector hierarchy?
10. Are there any political considerations that could give rise to greater risk of fraud?
11. Do laws and regulations contain requirements for political neutrality related to the use of resources and funds, and what is past experience in this area?

Laws, Regulations and Other Relevant Authorities

1. Is it clear which laws, regulations and authorities apply to the audited entity and the particular subject matter?
2. Are there overlaps or inconsistencies between different sets of legislation?
3. Is the entity a law making body, and if so what impact can the law making process have on the rights of individuals?
4. If the entity is a law making body, has it delegated any authority to other entities, such as regulatory authorities or private sector entities?
5. Is relevant legislation relatively new, or is it well established?
6. If new, is it clear in terms of form and content such that it may be clearly understood and applied?
7. If well established, has legal precedent been consistent such that the legislation is clearly understood and applied?
8. Is the relevant program area subject to significant application of judgement in its operations?
9. If a significant amount of judgement is applied, is this done in accordance with the intentions behind the laws and regulations?
10. If a significant amount of judgement is applied, is it applied consistently?
11. Are other bodies involved in interpreting or supplementing the relevant legislation?
12. Has the entity carried out its duties on a timely basis such that individual rights have not been compromised, and there have not been significant negative financial consequences due to passiveness?
13. Have channels for complaints and appeals for affected parties been used appropriately?
14. Have any individual's / organisation's rights been compromised in any way through the entity's interpretation and application of particular legislation or regulations?

15. Are there any aspects of laws, regulations or other authorities that could give rise to greater risk of fraud?

Significant Events and Transactions

1. Are there any significant events or transactions that may give rise to significant risks or fraud risks (e.g. significant procurement contracts, long term construction contracts, dealings in financial instruments such as foreign exchange contracts, significant loans or financial speculation, privatisation etc)?
2. Does the entity possess the necessary authority and competence to enter into and carry out significant events and transactions?
3. Have experts been engaged in connection with significant events and transactions?
4. If experts have been engaged, what precautions have been taken to ensure their competence and objectivity?
5. How is the work of experts monitored?

Management

1. Is there stability in the management team or have there been changes in key personnel?

2. How are members of management recruited (open and transparent processes with real competition, or token process)?

3. Is management actively involved in assessing risk on a continual basis?

4. Has management considered the consequences of changes in the entity's environment and the impact this may have on the audited entity?

5. Is management conservative in its approach or more willing to take risks (e.g. what is the 'risk appetite')?

6. What initiatives has management taken to identify and avoid significant risks that could have an adverse impact on the entity?

7. Are risk evaluations that are performed throughout the entity effectively communicated to management at the appropriate levels?

8. Does management actively monitor and evaluate the consequences of their decisions and actions?

9. Have previous audits identified instances of non-compliance, fraud, unlawful acts, unethical behaviour, management bias, etc?

10. How does management balance the achievement of program objectives with the need to manage risk, and ensure compliance with laws and regulations etc?

Appendix 4 Examples of Risk Factors Related to a Particular Subject Matter

Procurement is a typical subject matter for compliance audits. The following table gives some examples of risk factors relating to a compliance audit of procurement. The list is not intended to be exhaustive. The relevant risks and risk factors will vary depending on the subject matter and the circumstances of the particular audit.

Examples of Risk Factors Related to the Audit of Procurement	
Inherent risk	
1	Lack of relevant procurement legislation
2	Recent changes to the procurement legislation (eg to conform to international legislation)
3	Complex or unclear legislation, or legislation open for interpretation
4	Significant monetary amounts are involved such as defence procurement
5	Audit findings from the prior year revealed compliance deviations in regard to procurement legislation and directives
6	Previous suspicions or instances of fraud and corruption involving management and key staff
7	Inspections by regulatory authorities (eg competition authorities)
8	Complaints received from potential suppliers about unfair practices related to awarding tenders
9	Potential conflicts of interest
Control risk	
1	Lack of good internal guidelines, including lack of clear and objective criteria
2	Recent changes in general or application controls related to procurement IT systems
3	Poor quality-control or weak monitoring activities related to suppliers

4	Weak or non-existent controls regarding suppliers' compliance with ethical guidelines
5	Non-existent or poor quality monitoring activities related to compliance with relevant legislation
Detection risk	
1	Audit procedures are ineffectively designed (eg performing procedures that only involve checking transactions that are recorded, and not checking for completeness; or making inquiries only of staff in the procurement department and not of others such as administration or facilities management staff, suppliers or agencies that register complaints)
2	Incentives may lead management to intentionally withhold or conceal evidence (for example, suppliers may make bribes or give kickbacks)
3	Possible management collusion or override of controls

Appendix 5 Examples of Compliance Audit Procedures for Selected Subject Matters

This table shows illustrative examples of possible compliance audit procedures in the areas of environmental legislation and project funds from donor organisations. It is not intended to be an exhaustive list of procedures. Audit procedures must be designed for the particular audit circumstances and objectives.

Sample audit procedures	
Subject matter: Environmental legislation	
1	Obtain an overview of relevant environmental legislation to which the entity is required to adhere.
2	Inquire with management, and internal audit as applicable, as to the processes and routines in place to ensure compliance with relevant environmental legislation.
3	Review manuals and systems descriptions to understand the processes and relevant controls. Document the process and identify key controls. Test key controls as necessary.
4	Perform a media search, and other databases as applicable, to identify previous instances of non-compliance by the entity.
5	Review any inspection reports, including those of internal audit as applicable. Follow up any areas that may indicate significant risks of non-compliance with environmental legislation.
6	Confirm that the audited entity has necessary permits and registration certificates as appropriate. Evaluate procedures to ensure that these remain valid and up to date.
7	Review minutes of meetings of environmental, or health and safety committees. Follow up as necessary.
8	Interview selected staff as to their understanding of relevant policies and procedures in place, including training, and how these procedures operate in practice.

9	Inquire with management, and legal counsel as appropriate, as to any previous, existing or potential environmental liability claims. Consider the causes and effects/impacts of any such claims.
10	Observe processes and routines in practice (eg waste disposal – properly stored and disposed of, etc) and document appropriately (eg photo or video evidence may be relevant)

Sample audit procedures

Subject matter: Project funds received from a donor organisation

1	Obtain an overview of the funding agreement and any relevant legislation, directives, mandates, etc to which the entity is required to adhere.
2	Inquire with management, and internal audit as applicable, as to the processes and routines in place to ensure compliance with the terms of the funding agreement and relevant legislation, directives, mandates, etc. Inquire as to routines to ensure appropriate accounting and disclosure.
3	Review manuals and systems descriptions to understand the processes and relevant controls related to compliance with such funding agreements. Document the process and identify key controls. Test key controls as necessary.
4	Perform analytical procedures for assessing risks, and substantive procedures as considered necessary. For example, compare any financial information, including project accounts, with budget and prior year(s). Follow up suspected deviations as necessary in the circumstances. Review project accounts for unusual or significant transactions. Follow up as necessary.
5	Select a sample of transactions related to project funds. For each transaction selected, test compliance with the terms of the funding agreement and any relevant legislation, for example: • requirements related to use of funds • proper approval and authorization • reporting requirements • proper accounting and disclosure, including appropriate accounting policies and recording transactions in the appropriate periods, etc.

6	Where project funds have been used for specific purposes, assess the need to perform physical inspections. Follow up as appropriate.
7	Review related correspondence, minutes of meetings etc to identify any relevant matters. Follow up as necessary.
8	Consider the need to obtain any written confirmations from third parties and follow up as appropriate.
9	Consider the need to obtain specific written representations from management in regard to the funding agreement.
10	Perform cut-off testing and review after the period end as necessary to ensure funds are accounted for in the appropriate period.

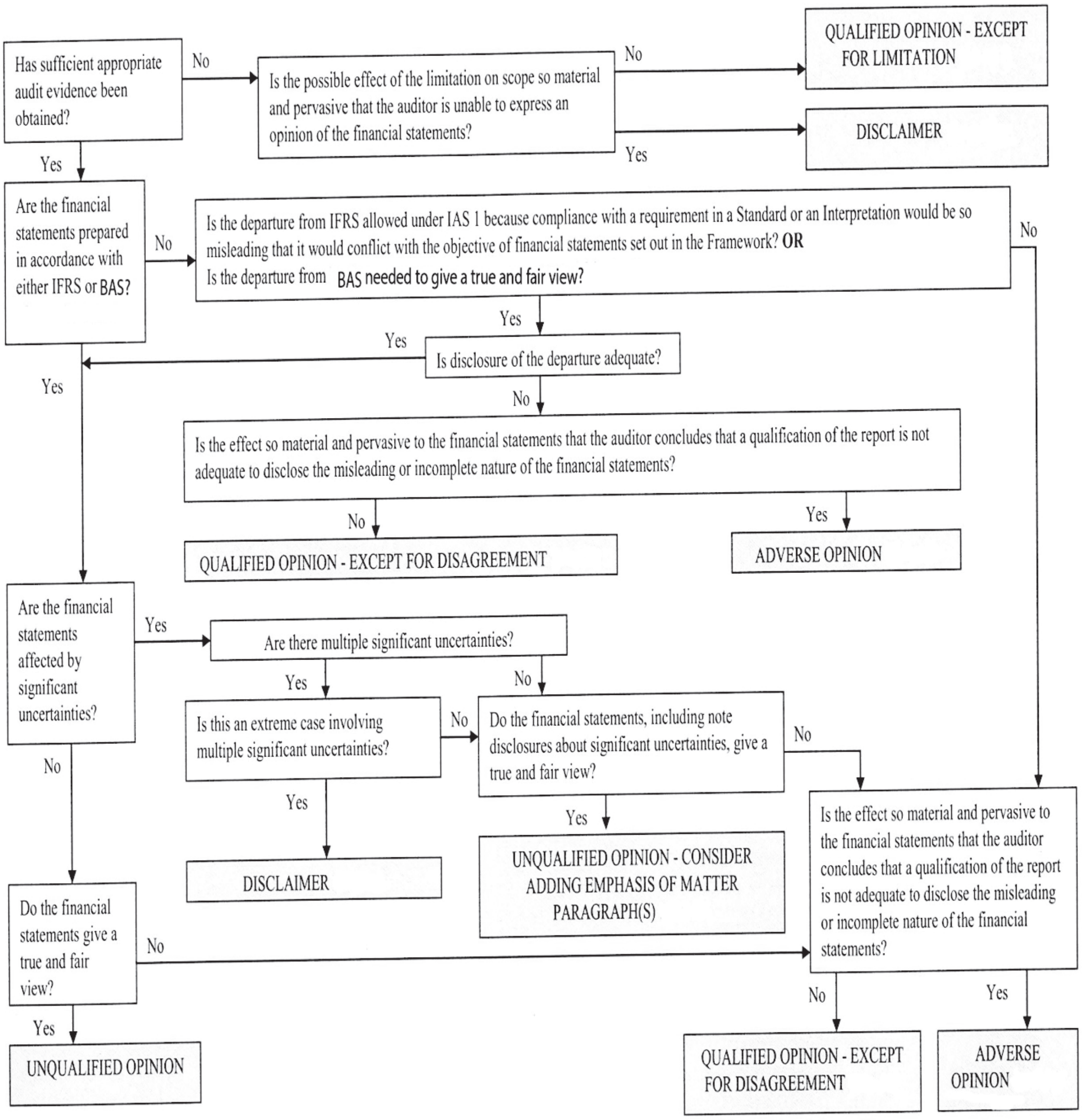
Appendix 6 Examples of Compliance Deviations

The following table provides some examples of compliance deviations and includes considerations related to materiality and forming conclusions. The comments related to materiality and forming conclusions are not intended to be definitive assessments of whether the particular example constitutes a material compliance deviation or not, but rather to highlight relevant considerations. The determination of materiality will depend on the particular circumstances and the professional judgement of the public sector auditor.

Example of Compliance Deviation		Considerations Related to Materiality and Forming Conclusions
1	During the year, a government agency received budget appropriations through the Ministry of Education for national educational purposes. The agency's grant expenditure for the year included TK. 1 Crore to overseas high tech manufacturers.	Based on the legislation governing the government agency, the agency did not have the power to make grants to overseas bodies. The non-compliance may be material because the grant expenditure was paid out to overseas bodies and was therefore not in compliance with relevant authorities, nor was it applied to the purposes intended by the legislature.
2	During the year, a government agency incurred expenditures of TK. 100 in excess of the total expenditure of TK. 5000 authorised by the budget approved by the legislature.	In this case, actual expenditures were in excess of amounts authorised through the approved budget. This non-compliance may be material because it was a clear violation of clearly established authorities. Depending on the circumstances, including the type of expenditures, it may also be very sensitive in nature.
3	A citizen is entitled to a monthly pension of TK. 1000. The government agency has only been paying out TK. 900 per month. The payments were also made after the dates stipulated in the legislation.	Although the monetary amounts involved may not be material to the financial statements of the government agency, the consequences of the noncompliance are likely to be very significant to the individual pensioner living on a fixed income. If the non-compliance is due to a system weakness, the non-compliance may also affect many other citizens. The non-compliance may therefore be material in terms of the impact on citizens and society in general.
4	A single mother is entitled to monthly child benefits for each child under age 18. The government agency has paid out	While this compliance deviation may have been positive for the recipient, it is not in accordance with the legislation and its intentions, and may therefore be unfair to other beneficiaries. If the

	Example of Compliance Deviation	Considerations Related to Materiality and Forming Conclusions
	child benefits for a 19 year old child.	non-compliance is due to a system weakness, the non-compliance may also affect many other citizens. The non-compliance may therefore be material in terms of the impact on citizens and society in general.
5	The terms of a building code require annual inspections to be performed. The government agency has not performed inspections for the past five years.	The non-compliance may be significant due to qualitative aspects such as safety implications. Although no particular monetary amounts are involved, the non-compliance may be material due to the potential consequences it may have on the safety of the building occupants. In the event of a disaster, there is also a risk that the noncompliance may result in significant liability claims which could have material financial implications for the government agency as well.
6	The terms of a funding agreement state that the recipient of the funds must prepare financial statements and send them to the donor organisation by a certain date. The financial statements have not been prepared and sent by this date.	The non-compliance may or may not be material depending on whether or not the financial statements were subsequently prepared and sent, the extent of the delay, the reasons for the delay, any consequences that may arise as a result of the non-compliance, etc.
7	Significant system weaknesses were identified in relation to revenues collected in accordance with a tax code. The weaknesses were due to incorrect interpretation of the tax code by the audited entity. Numerous instances of taxpayers being assessed more than they were obligated to pay were identified.	This type of compliance deviation relates to the due process rights of individual citizens. Certain citizens were being assessed too much tax, while others were not being assessed at all. Depending on the circumstances, and because it involves a system weakness, the deviation may be material.

Forming an Opinion on Financial Statements[1]



[1] This flowchart does not cover modified reports involving going concern problems. Refer to the most recent version of the APB Bulletin, "Auditor's Reports on Financial Statements".

1. This diagram is adapted for our purposes from the version contained in ISA 700

Annexures

Overall Audit Strategy

This document is intended as a stand-alone document which sets our overarching audit strategy. It is used to frame an agenda of questions for the initial planning meeting between the Director General or Director, Manager and any other invited audit team members, to set the high level strategy. It is also used to record the decisions reached about the scope, timing and direction of the audit and how the more detailed audit plan should be developed.[5]

The Overall Audit Strategy should identify from our existing understanding the Significant Risks for the audit, and the risk assessment procedures required refreshing, extending or confirming our existing understanding and identifying any further risks for our audit. A Significant Risk is defined in the ISAs as "an identified and assessed risk of material misstatement that, in the auditor's judgement, requires special audit consideration."

The significant risks section is at the start of this document for ease of reference throughout the audit. However, teams must ensure that the factors contained in all sections of this document are given proper consideration in identifying and assessing risks.

The form should not be used to replicate information from detailed planning documentation – it should be focused on only the key information and issues for the audit.

A. What are the Significant Risks for our audit and how will we respond to them?

In planning our response to Significant Risks, consider:

- identifying the classes of transactions, account balance, or disclosures as precisely as possible (e.g. payments during particular periods, transactions with certain counterparties, assets held in particular locations, etc);
- identifying how management get comfort over the risk and test related controls or plan procedures to earn the right to rely on the output of their procedures as part of our overall assurance;
- testing transactional level controls that mitigate the specific risk;
- using external confirmations (including to confirm contractual terms or the absence of side-agreements as part of our assurance);
- using Computer Assisted Audit Techniques to identify items potentially affected by the risk; and

[5] *Considerations for establishing the Overall Audit Strategy are included in the Appendix to ISA 300, (and examples of fraud risk factors which may be relevant to consider are included in the Appendices to ISA 240.)*

- using specialist or more experienced staff to carry out the audit procedures addressing Specific Risks or the audit as a whole in the case of Pervasive Risks.

What are Pervasive Risks, including risks of fraud, which affect our approach at an overall financial statement level? *(e.g. significant reorganisation of the entity's finance function, implementation of a new financial system, issues over going concern)* What are our planned responses?

-

Pervasive risk	Parent risk（P）, group risk（G）or both?（N/A if not a group audit）	Controls which address the risk and planned extent of controls work（at minimum D&I）	Planned overall responses
Fraudulent Financial Reporting			

Are there additional risks of management override of control beyond those included in ISA 240? Are there any specific considerations for how we should perform the required responses? Are there any additional responses required?

Risk of management override through	Controls which address the risk and planned extent of controls work（at minimum D&I）	Planned overall responses?
Journals		
Significant unusual transactions		
Bias in accounting estimates		

What are the Specific Risks, including risks of fraud, affecting specific classes of transactions, account balances and disclosures? Which assertions are affected, and what is our planned response?

-

Specific Risk	Parent risk (P), group risk (G) or both? (N/A if not a group audit)	Audit area(s) and component(s) affected	Assertion(s) affected	Controls which address the risk and planned extent of controls work (at minimum D&I)	Planned substantive procedures (and other responses as appropriate)

If we have not identified a Specific Risk of fraud in revenue recognition, how will we rebut the presumption of this risk in ISA 240?

THE ENGAGEMENT TEAM SHOULD TRANSFER THE SIGNIFICANT RISKS IDENTIFIED TO THE SIGNIFICANT RISKS TESTING PLAN. THIS LIST SHOULD BE UDPATED IF ANY ADDITIONAL SIGNIFICANT RISKS ARE IDENTIFIED, AND THE APPROACH AGREED WITH THE DIRECTOR GENERAL OR DIRECTOR AND MANAGER. ANY RISKS WHICH ARE NOT SIGNIFICANT (AND ARE ADEQUATELY COVERED BY STANDARD AUDIT PRODECURES) BUT WHICH THE ENGAGEMENT TEAM CONSIDERS NECESSARY TO DOCUMENT AT THIS STAGE SHOULD BE ENTERED AS RISK FACTORS IN SECTION H.

B. What do we understand about the reporting entity[6]?

What is the nature of the entity?

ACCOUNT TYPE	

What are the statutory objectives and remit of the organisation?

-

What are the entity's associated organisational objectives and strategies?

-

What are the key elements of the general framework of authorities for the entity? Is there a risk of irregular or novel and contentious transactions?

-

What are the key elements of the statutory framework on specific benefits, grants, services and income?

.

Have there been any significant changes in the period, including any new statutory activities (e.g. new grant schemes, statutory functions)?

-

What are the key performance measures which might indicate a risk to the manipulation of financial reporting (including financial KPIs)?

-

What issues were identified in the prior year management letter, and are we aware of any progress in resolving these issues?

-

What else do we understand from other audit work relevant to the entity?

-

[6] Group auditors should complete this form in respect of both the group and parent/core department, and also complete Appendix A, Group Audits.

C. What do we understand about the entity's internal controls?

What are the key features of our understanding of the entity's internal control?

(*This may cover: the "tone from the top" and quality of the overall control environment; the entity's risk assessment processes and the output of these processes; the entity's information systems and processes including the financial reporting process; and how the entity monitors its internal control systems)*

-

Are there any concerns about the processes and controls in place to ensure the regularity of transactions? Are there any concerns about propriety of transactions?

-

Does the entity's internal control support the reliable processing of financial information?

- .

Are there areas where we need both controls and substantive assurance to obtain sufficient appropriate audit evidence (e.g. high volume automated transactions, regularity in complex frameworks of authorities)?

-

Do we plan to rely on tests of controls as part of our audit approach?

-

If we are planning on relying on high level controls for assurance, what procedures will we perform to evidence that the controls are sufficiently precise to mitigate the risk of material misstatement in each area we plan to rely upon?

-

Are we planning to rely on controls which are dependent upon the IT systems? If so, how will we gain assurance over the design, implementation and operation of IT controls?

-

What is our understanding about internal audit's role in the organisation and its relevance to the financial audit?

-

Do we plan to rely on the work of internal audit? What procedures do we need to perform to earn the right to rely on their work?

-

D. What is our understanding of the entity's financial reporting?

What is the entity's financial reporting framework?

Accounting framework	

Will we issue a regularity opinion?

Are there any complex or specialised accounting issues for the entity?

-

What is our understanding of the quality of the entity's financial reporting and close process, including associated controls?

-

What is the historical level of errors identified through our audit?

-

Are there any issues relating to the appropriateness of the entity's selection and application of accounting policies, including changes to these policies?

-

Are there any issues relating to the appropriateness of the entity's selection and application of methods of making accounting estimates, including changes to these methods?

-

Are there any issues relating to non-standard disclosures? ***(Not in conformity with Generally Accepted Accounting Procedures)***

-

What is our understanding of the quality of the entity's controls over the regularity of transactions?

-

What is the historical level of irregularities identified through our audit?

-

E. What is material to the entity's financial statements?

What are appropriate bases to consider in setting materiality?

-

What qualitative factors should affect our assessment of materiality?

-

What is the level of total anticipated error for the accounts which should be used in setting Performance Materiality?

-

Are there items which we would expect to be material by nature or context and for which we intend to set a lower materiality and Performance Materiality?

-

USE THE MATERIALITY ASSESSMENT FORM TO ESTABLISH PLANNING MATERIALITY AND PERFORMANCE MATERAILITY AS PART OF ESTABLISHING THE OVERALL AUDIT STRATEGY

F. Other issues

Are there any significant accounting estimates?

-

Do we plan to rely on the work of management's experts? What procedures do we need to perform to earn the right to rely on their work?

-

Do we plan to rely on the work of our own experts? What procedures do we need to perform to earn the right to rely on their work?

-

Do we plan to use any assistance from our framework partners (other than use of experts)?

-

What are the factors affecting the going concern assessment? What procedures do we need to perform in respect of this?

-

Are there any concerns with respect to commitments and contingencies? What procedures do we need to perform in respect of this?

-

Are there any concerns with respect to laws and regulations? What procedures do we need to perform in respect of this?

-

Are there any concerns with respect to related party transactions and disclosures? What procedures do we need to perform in respect of this?

-

Are there any particular considerations around handling personal data that the engagement team should be aware of? In particular, will we need to handle high volume or high sensitivity personal data?

-

Are there any issues around our independence which should be considered in planning the engagement?

-

Are there any other issues which should be considered in planning or performing the engagement?

(e.g. security clearances, audit protocols, client liaison contacts, etc)

-

G. What are the key issues from the client's perspective?

Understanding the client's key concerns can assist in identifying Significant Risks to the audit which we were otherwise unaware of. It may also identify ways, in the context of an efficient audit approach, of adding value by providing more detailed reporting of our findings or through reasonable extensions of our procedures to address their concerns. In addition, promoting improvements in internal control may produce audit efficiencies going forward (or in the current year).

Who are the key client personnel, and what relationship do we have with them?

Name	Role	Comments

What concerns the Accounting Officer, the Finance Director and the Audit Committee Chair?

(In particular, what concerns the Accounting Officer about delivering the entity's objectives, the Finance Director about financial reporting and controls, and the Audit Committee Chair about the entity's governance? What is their view of the key risks facing the entity? How do they get comfortable over the risks with financial statement impact?)

-

What concerns the entity's key stakeholders?

-

What are the expectations of key client personnel from the audit and the OC&AG generally?

-

What actions, if any, in our audit approach would address client or stakeholder concerns and expectations, or otherwise add value? How can we promote beneficial change in the entity's financial management and reporting, conduct and provision of services?

Action	Allocated to

H. What other risk factors have we identified?

(Risk Factors are either:

- *risks of material misstatement or irregularity which are addressed through standard planned testing over the relevant assertions, and so do not require any additional specific audit response; or*
- *potential risks which have been assessed as not representing a risk of material misstatement/irregularity, and so do not require an audit response.*

Risk Factors may include business risks with an operational impact but without a direct impact on the financial statements.)

What other risk factors have we identified that the engagement team should consider as the audit progresses?

This consideration will normally not involve additional procedures, but represents part of maintaining an attitude of professional skepticism. The list should include fraud risk factors (ISA 240 para 11 "events or conditions that indicate an incentive or pressure to commit fraud or *provide an opportunity to commit fraud.”). However, any risks of material misstatement due to fraud should be treated as Significant Risks.*

Risk Factor	Pervasive / Assertions affected	Comments on why considered only a Risk Factor	Additional Procedures required (if any beyond consideration by the team of its potential impact as the audit progresses)

THE ENGAGEMENT TEAM SHOULD TRANSFER THE OTHER RISK FACTORS IDENTIFIED TO THE AUDIT AREA TESTING PLAN. THIS LIST SHOULD BE UDPATED IF ANY ADDITIONAL RISK FACTORS ARE IDENTIFIED DURING THE AUDIT, AND THEIR ASSESSMENT AS A RISK FACTOR RATHER THAN SIGNIFICANT RISK AGREED WITH THE DIRECTOR AND MANAGER.

I. What risk assessment procedures are required?

<u>This section would be expected to be completed on a “by exception” basis</u>

ISA 315 requires the performance of risk assessment procedures to identify and assess the risks of material misstatement. Where we are familiar with the entity, we may be able to use information obtained from our previous experience with the entity and from previous audits, subject to the requirement in ISA 315 para 9 to “determine whether changes have occurred since the previous audit that may affect its relevance to the current audit.” This may be by inquiry alone, or, where appropriate, by performance of other appropriate audit procedures.

Step in the Risk Assessment Procedures	Planned approach (be as specific as possible)
Preliminary Analytical Procedures	
Understanding the Entity and its Environment	
Relevant industry, regulatory, and other external factors	
The nature of the entity and its activities	
The entity's financial reporting and accounting policies	
The entity's objectives and strategies, and related business risks.	
The measurement and review of the entity's financial performance.	
The nature and extent of the entity's related party relationships	
Understanding the Entity's Internal Control	
Control Environment	
The entity's risk assessment process	
Monitoring of controls	
Business controls	
The information system	
Communication	
Controls relevant to the audit (evaluation of design and implementation required each year)	
▪ Controls addressing Significant Risks	

Step in the Risk Assessment Procedures	**Planned approach (be as specific as possible)**
▪ Controls we intend to rely on in our audit	
▪ General IT controls (where we plan to test their operating effectiveness)	
▪ Financial reporting process controls	
▪ Governance Statement controls	
▪ Overall regularity controls	
▪ Other controls – detail any required	
Required planning inquiries	
Management	
Those Charged with Governance	
Internal Audit	
Others e.g. in-house legal council, operational staff	
Identify significant classes of transactions, account balances and disclosures	
Identification process	
IT Scope assessment	
Identify any IT risks	
Identify any controls we plan to rely on dependent upon general-IT controls	
Fraud Risk assessment	
Identify any fraud risk from our planning not already identified	

J. What else should we consider in planning our audit approach?

(excluding our responses to Significant Risks, which are discussed above)

<u>This section would be expected to be completed on a "by exception" basis</u>

Will the client perform a hard close? What work should we perform on the hard close?

(A "hard close" is a month-end close performed with the same rigour as a year-end close, which enables balance sheet and income testing at an interim date, with e.g. substantive analytic procedures used to provide assurance over the year-end balance sheet position)

-

If the client will not be performing a hard close, is it still appropriate to perform testing at an interim date? What work should be performed at interim?

(Any planned work should reflect the quality of the close process – e.g. we may not be able to get assurance over accruals or accrued expenditure at interim)

-

Which classes of transactions, account balances and disclosures do we plan to obtain controls assurance over? Which controls are suitably precise to provide the assurance required?

-

Are there Audit Areas where it would be appropriate to use external confirmations?

(Other than bank circularisation of cash at bank, overdrafts, and bank loans – these are required for all accounts other than Government Banking Service accounts)

-

Are there Audit Areas where Computer Assisted Audit Techniques can provide either additional or more efficient assurance over the balance?

- IDEA transaction sampling

Are there other aspects to our approach to testing Audit Areas that should be specified as part of the Overall Audit Strategy?

(Comment by exception where the Director General or Director wishes to specify an approach ***– e.g. specific tests over regularity of grants, areas where substantive analytic procedures would be more appropriate than tests of details, etc)***

-

K. What engagement team do we need?

Do we need to involve specialists in any areas of the engagement

-

Who are the key members of the engagement team?

Name	Role	Relevant skills knowledge and experience	Years on engagement
	Assignment Director		
	Audit Manager		
	Overall Team Lead		

L. What is the reporting timetable?

Date	Key stage of the audit
	Central planning meeting
	Mission Planning
	Field work
	Receipt of first draft accounts
	Receipt of signed accounts
	Audit opinion to be signed
	Draft Report/Management letter to be sent

Financial and Compliance Audit Planning Checklist

Instructions

This checklist is for recording the progress and completion of the audit plan. The only element of planning which will need to be completed subsequently in the electronic working paper system is the importing of standard testing work programmes and addition of any customised tests.

In the table below, document the date each planning activity task has been completed, name of the audit team member who has completed it, any relevant notes (including conclusions) and attach any relevant papers which are necessary.

	Activity	Initials	Date completed or N/A	Notes	Link/ attachment
	A1: Preliminary Engagement Activities Perform procedures to ensure that we can perform the audit.				
1) **Engagement Activities: New clients**	For all new audits ensure that: • the Director or Director General's consideration of whether the audit should be accepted is documented; and • the C&AG has approved acceptance of the engagement.				
2) **Delegated Authority**	Consider whether delegated signature of the certificate/audit report is appropriate for the audit, and if so consider whether the relevant C&AG approval has been granted.				
3) **Engagement Activities: Continuing clients**	For all continuing clients update the Engagement Risk Management Checklist.		[		
4) **Letter of Engagement/ Understanding**	Issue a revised letter of engagement/ understanding. Ensure a signed copy of the letter of engagement / understanding is held on file.				
5) **EQCR**	Consider whether the audit requires an External Quality Control Review and request that one is appointed if necessary.			EQCR required where:	

				• the Director or Director General expects to remove a long standing qualification, i.e. where the accounts have been qualified in respect of more than one period for a recurring reason; • the largest and most complex accounts; or • where there are unusual circumstances or risks in an audit.	
	A2: Overall Audit Strategy The Engagement Director must establish an Overall Audit Strategy				
6) Client Planning Enquiries	Make enquiries of the key client contact(s) relevant to the forthcoming audit.				
7) Preliminary	Perform preliminary analytical procedures as determined in the Overall Audit Strategy,				

Analytical Procedures	including at least one the following items: ▪ Identification of new revenue and expenditure streams; ▪ the performance measures against which the entity is assessed and the impact that these may have on the reported results of the organisation; and ▪ a comparison of the draft financial statements (or projected figures) against the prior year's figures, including examination of trends. Determine whether the findings indicate any additional significant risks to the audit.				
8) Materiality	Determine materiality and performance materiality (Financial and Compliance Audit Annex H and H.1)				Materiality Determination Form Annex H.1 **MANDATORY**
9) Overall Audit Strategy	Hold an overall audit strategy meeting, which must be attended by the Director General or Director and Manager (others at the invitation of the Director General or Director). This meeting may be led by a facilitator but if not, will be led by the Director or General Director. Record the Overall Audit Strategy and record here the Director's approval of the Overall Audit Strategy.				OAS Annex A **MANDATORY**

10) Risk Assessment Procedures	As part of the Overall Audit Strategy, determine and document what further Risk Assessment Procedures are required.				OAS **MANDATORY**
	A3: Risk Assessment Procedures				
11) Inquiries	Perform required inquiries of: 1. Management 2. Internal audit; and 3. Others as appropriate.				
12) Evaluate the work of Internal Auditor	Understand the work that Internal Audit plans to perform, and any findings to date, to identify whether there are opportunities to use their work, or whether they are indicative of further significant risks: 1. Review the Internal Audit Plan for the year and any relevant reports currently available. 2. Document our consideration of the plan and the reports issued so far.				

13) Understanding the Entity and its Environment	Update our understanding of the entity and its environment, sufficiently to inform our risk assessment.				Annex B **MANDATORY**
14) Understanding the Entity's Internal Control	Update our understanding of the entity's internal control, sufficiently to inform our risk assessment. This may include updating the system notes of the client's key financial reporting and related systems.				Annex C **MANDATORY**
15) IT Risks	Consider whether there are any further indications of significant risks related to IT.				IT Scope Assessor Annex D **MANDATORY**
16) Fraud Risks	Consider whether there are any further indications of significant risks of fraud.				Fraud Risk Assessment form Annex E **MANDATORY**
17) Brought forward accounting judgements	Consider whether there are any historic accounting judgements which will have a significant impact on the current year financial statements. Ensure that any relevant documentation supporting these judgements is brought forward as standing information to be assessed and updated later in the audit process (this may include technical papers, evidence of liaison with clients).				
18) Conclude on	Conclude as to whether our risk assessment procedures have identified any further				

new risks	significant risks or changed our assessment of risks identified in the Overall Audit Strategy. If any changes are required to the Overall Audit Strategy, these should be included and a revised version filed following discussion and approval by the Director or Director General. This may be done by updating the original form and highlighting changes on that document. However if there are many changes, a separate document may be required to log each amendment to the Overall Audit Strategy and ensure it is approved by the Director or Director General.				
	A4: The Audit Plan Document and agree the planned responses to significant risks and the planned responses to areas not affected by significant risks.				
19) Audit Plan	Produce an audit plan to respond to the significant risks (in the SRTP) and the audit areas not affected by significant risks (in the AATP) using standard testing programmes from the Testing Options Support Tool wherever possible.				SRTP Annex F & AATP Annex G - both **MANDATORY**
20) Director's	Confirm the Director's approval of the planned				Step in Electronic Working papers

Approval of Plan	procedures which are included in the SRTP and AATP.				system
21) EQCR Review of the Audit Plan	Confirm External Quality Control Review of the audit plan, attach a copy of the EQCR's comments and their approval of the plan.				
22) Audit Planning Report	Produce and submit an Audit Planning Report to the client.				
23) Project Planning with Client	Agree relevant details of how the audit will be performed with the client. This should not include the detail of our planned testing approach, but should normally cover: • the audit timetable; • information request lists; • personal data requests; and • any other aspects of the audit plan dependent upon co-ordination with the client.				

	A5: Administrative Matters				
24) Admin	Complete the following administrative tasks: . Establish a budget. • Where relevant agree a fee with the client. • Complete the planning section of a personal data processing form. • Ensure that the client is aware of the OCAG policy on personal data handling. • A privacy impact assessment has been completed where appropriate. • Document the declarations of team members' independence.				
25) Team Briefing	Hold a team briefing for all team members who did not attend the Overall Audit Strategy meeting. The briefing should include discussion of the risk of material misstatement including those due to fraud. If not all team members are				

	able to attend (including specialists in the engagement team), document how the Director General or Director has determined the matters discussed should be communicated to those not attending.				

Annex A.2.1-

Compliance Audit Letter of Engagement Template

Government of The people's Republic of Bangladesh
[Insert Address of Auditor]

[Insert Address of Auditee]

Subject: Letter of engagement regarding the compliance audit of [Insert Name of Entity]

Reference:

Sir,

1. INTRODUCTION

1.1 The purpose of this letter is to set out the basis on which the Comptroller and Auditor General (C&AG) audits the **[Insert details of activities being audited]** of the **[Insert Name of Entity]** and the respective responsibilities of the Secretary of the **[Insert Name of Entity]** as Accounting Officer and the OCAG, acting on behalf of the C&AG. This engagement will be conducted with the sole objective of our expressing an opinion on **[Insert Name of Entity]**'s compliance with **[Insert details of legislation or other regulations that govern the activities being audited]**.

The terms of the audit engagement are set out below. This letter will remain effective until a new audit engagement letter is issued.

2. SCOPE OF THE AUDIT

2.1 The compliance audit will be conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAIs) and will cover the **[Insert details of activities being audited]** for the **[Insert Name of Entity]** for the financial year **[Insert Financial Year]**.

3. Responsibilities of auditors

3.1 The C&AG audits the **[Insert details of activities being audited]** under Article 128(1) of the Constitution of Bangladesh which states that the public accounts of the Republic and of all courts of law and all authorities and officers of the Government shall be audited and reported on by the Auditor-General and for that purpose he or any person authorized by him in that behalf shall have access to all records, books, vouchers, documents, cash, stamps, securities, stores or other government property in the possession of any person in the service of the Republic, and section 5(1) the Comptroller and Auditor General (Additional Functions Act) 1974 which states that the Auditor-

General may audit the accounts of any Statutory Public Authority (public enterprise) or local authority and shall submit his report on such audit to the President for laying it before Parliament. **[PLEASE ALSO INCLUDE DETAILS OF ANY OTHER RULES, LAWS AND REGULATIONS APPLICABLE TO THE SCOPE OF THE COMPLIANCE AUDIT]**

3.2 Consequently, the C&AG is responsible for reporting whether in his opinion the **[Insert details of activities being audited]** of **[insert name of entity]** are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the expenditure and income have been applied to the purposes intended by the legislature. Such procedures include the assessment of the risks of material non-compliance.

4. The compliance audit process

4.1 The audit will be conducted in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). These Standards require that we comply with ethical requirements and plan and perform our audit to obtain reasonable assurance of detecting errors, irregularities and illegal acts.

4.2 We shall obtain an understanding of the accounting and internal control systems to assess their adequacy as a basis for the preparation of the **[Insert details of activities being audited]** and to establish whether proper accounting records have been maintained by the **[name of entity]**. We shall expect to obtain such appropriate evidence as we consider sufficient to enable us to draw reasonable conclusions therefrom.

4.3 The nature and extent of our procedures will vary according to our assessment of the **[Insert name of entity]** and, where we wish to place reliance on it, the internal control system, and may cover any aspect of the operations that we consider appropriate.

4.4 Limitations of a compliance audit

4.4.1 We will plan our audit so that we have a reasonable expectation of detecting material instances of non compliance with relevant rules, laws and regulations in relation to the **[Insert details of activities being audited]** including those resulting from fraud, error or non-compliance with laws or regulations, but our examination should not be relied upon to disclose all areas of non compliance as may exist. Due to the test nature and other inherent limitations of compliance audit there is an unavoidable risk that some material misstatement may remain undiscovered.

4.4.2 Our work on internal control will not be sufficient to enable us to express any assurance on whether or not the **[Insert name of entity]** internal controls are effective. Our audit of the **[Insert details of activities being audited]** cannot be relied upon to draw to your attention all matters that may be relevant to your consideration as to whether or not the system of internal control is effective.

4.5 **Management representations**

As part of our audit process we will request from management written representations on matters material to the **[Insert details of activities being audited]** where other sufficient appropriate evidence cannot reasonably be expected to exist, and where management may have made certain oral representations (Letter of Representation).

4.6 **Reliance on third parties**

4.6.1 **Use of Experts**

Where we judge that it is appropriate to use the work of an expert we will-

- obtain sufficient appropriate audit evidence that such work is adequate for the purposes of the audit;
- evaluate the professional competence of the expert;
- evaluate the objectivity of the expert;
- ensure that the scope of the work of the expert is adequate for our purposes; and
- evaluate the appropriateness of the expert's work as audit evidence regarding the assertions being considered.

4.7 **Communications**

4.7.1 At the start of our audit, we may issue an Audit Plan, containing details of identified risks and planned audit work on the **[Insert name of entity]** for the coming year. This will detail where the audit team intends to make use of other auditors or experts.

4.8.2 At the end of each audit we will report formally to you on:

- Any significant weaknesses in, or observations on, the accounting and internal control system including areas of non compliance with applicable authorities;
- Errors and instances of non compliance with relevant rules, laws and regulations identified in the course of the audit (unless deemed clearly trivial);
- Uncorrected misstatements;
- Expected modifications to the audit report; and
- Any other matters of interest.

5. **CLIENT RESPONSIBILITIES**

5.1 Our audit will be conducted on the basis that the Secretary **[Insert name of entity]** and those charged with governance acknowledge and understand that they have responsibility for:

(a) For such internal control as the Secretary**[Insert name of entity]** and those charged with governance determines is necessary to enable compliance with applicable rules, laws and regulations; and

(b) To provide us with:

- Access to all information of which the Secretary **[Insert name of entity]** and those charged with governance are aware that is relevant to our audit such as records, documentation and other matters;
- Additional information that we may request for the purpose of the audit; and
- Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

6. AUDIT ARRANGEMENTS

6.1 Access to Data and Personal Data

As part of our audit work we may need access to personal data which the **[Insert name of entity]** holds. We will manage any personal data in accordance with the Statement on the Management of Personal Data at the OCAG (Annex 1).

6.2 Health and Safety

Members of the audit team will be in touch with relevant **[Insert name of entity]** to discuss practical arrangements and the timing of audit visits. However, we would appreciate your co-operation in relation to the provision of support for our employees covering health, safety and emergency arrangements applicable to your premises.

6.3.2 The **[Insert name of entity]** is also responsible for the controls over, and the security of their website. The examination of the controls over the maintenance and integrity of the **[Insert name of entity]**'s website is beyond the scope of our audit.

7. OTHER MATTERS

7.1 Use of Report & Confidentiality

Any formal report or other unpublished reports from us may not be provided to third parties. Such consent will be granted only on the basis that such reports are not prepared with the interests of anyone other than the **[Insert name of entity]** in mind and that we accept no duty or responsibility to any other party as concerns the reports.

7.2 Quality of service

We would like to provide you at all times with a high quality service to meet your needs. If at any time you would like to discuss with us how our service to you could be improved, please raise the matter immediately with me.

ACCEPTANCE:

8.1 Once agreed, this arrangement will remain effective for future years unless it is terminated, amended or superseded. Should you wish to discuss any aspects of this before signing at the foot of this letter and returning a copy, please do not hesitate to contact me.

Yours Sincerely,

Date:

Director General

For and on behalf of

The Office of the Comptroller and Auditor General

ANNEX- A.2.1.1: Statement on the Management of Personal Data at the OCAG

1. The CAG and the OCAG have privileged and wide-ranging access to data and information to support the discharge of the audit function and ensure that the OCAG's reports to Parliament are factual, accurate and complete. This data relates both to public servants and individual citizens. We have a duty to respect this privileged access and to ensure that the personal information entrusted to us is safeguarded properly.

2. We take our obligations for data protection seriously. We have a body of data policies and IT standards, guidelines and procedures designed to ensure data protection. We keep our requests for personal data to the minimum necessary to complete our work and retain any personal information we obtain only for as long as we need it. We take appropriate measures to safeguard the integrity and confidentiality of data we hold from unauthorised access. All of our staff and contractors have an obligation to comply with our data protection policies.

3. Our definition of sensitive personal data includes data which, when held alone or in combination, could cause embarrassment, harm or financial loss to the data subject if disclosed to or tampered with by an unauthorised third party. We have separate arrangements in place for classified data.

4. To help you understand our commitment, we have developed a series of Personal Data Statements, which all our staffs subscribe to:

   - We will only request personal data for use in discharging our statutory and other audit functions and for lawful purposes. These requests are kept to the minimum necessary to carry out our work.
   - Our requests for personal data will be authorised by a senior employee. Each of our audits is led by a Director or Director General who is personally responsible for authorising any request for personal data in connection with that audit; maintaining records of the data held; ensuring it is securely and appropriately processed; ensuring it is securely and appropriately retained; and for certifying its destruction.
   - We will agree with you in advance how we will use, secure, destroy and account for the personal data you provide to us. We have a series of protocols which specify the measures for protecting personal data during transfer from the information provider, whilst we retain the information for audit purposes, for secure destruction of the data and for long term storage where this is required by professional standards.

- We will notify you when we destroy personal data you have provided to us.
- We ensure our contractors operate suitable procedures for personal data protection before we pass such data to them. From time to time we contract with third parties who support us in discharging our responsibilities. Access to personal information will only be given to organisations which can show that they are capable of maintaining the standards defined in these statements.
- We audit our compliance with our data protection policies, in order to be assured that protection is in accordance with the terms of this Statement. These include checks on compliance carried out independently of the OCAG Directors responsible for the security of data on their audits.

Annex- A.2.2

Financial Audits Letter of Engagement

Government of The people's Republic of Bangladesh

[Insert Address of Auditor]

[Insert Address of Auditee]

Subject: Letter of engagement regarding the financial audit of [Insert Name of Entity]

Reference:

Sir,

1. INTRODUCTION

1.1 The purpose of this letter is to set out the basis on which the Comptroller and Auditor General (CAG) audits the **[Insert details of statements being audited]** of the **[Insert Name of Entity]** and the respective responsibilities of the Secretary of the **[Insert Name of Entity]** as Accounting Officer and the OCAG, acting on behalf of the CAG. This engagement will be conducted with the sole objective of our expressing an opinion on the **[Insert details of statements being audited]**.

The terms of the audit engagement are set out below. This letter will remain effective until a new audit engagement letter is issued.

2. SCOPE OF THE AUDIT

2.1 The financial audit will be conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAIs) and will cover the **[Insert details of statements being audited]** for the **[Insert Name of Entity]** for the financial year **[Insert Financial Year]**.

3. Responsibilities of auditors

3.1 The CAG audits the **[Insert details of statements being audited]** under Article 128(1)of the Constitution of Bangladesh which states that the public accounts of the Republic and of all courts of law and all authorities and officers of the Government shall be audited and reported on by the Auditor-General and for that purpose he or any person authorized by him in that behalf shall have access to all records, books, vouchers, documents, cash, stamps, securities, stores or other government property in the possession of any person in the service of the Republic, and section 5(1) the Comptroller and Auditor General (Additional Functions Act) 1974 which states that the Auditor-General may audit the accounts of any Statutory Public Authority (public enterprise) or local authority and shall submit his report on such audit to the President for laying it before Parliament.

3.2 Consequently, the CAG is responsible for reporting whether in his opinion the **[Insert details of statements being audited]** give a true and fair view and whether the activities, financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the agency's expenditure and income have been applied to the purposes intended by the legislature. Such procedures include the assessment of the risks of material non-compliance.

4. The financial audit process

4.1 The audit will be conducted in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). These Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance over whether the **[Insert details of statements being audited]** are free from material misstatement.

4.2 We shall obtain an understanding of the accounting and internal control systems to assess their adequacy as a basis for the preparation of the **[Insert details of statements being audited]** and to establish whether proper accounting records have been maintained by the **[name of entity]**. We shall expect to obtain such appropriate evidence as we consider sufficient to enable us to draw reasonable conclusions there from.

4.3 The nature and extent of our procedures will vary according to our assessment of the **[Insert name of entity]** and, where we wish to place reliance on it, the internal control system, and may cover any aspect of the operations that we consider appropriate.

4.4 Limitations of a financial audit

4.4.1We will plan our audit so that we have a reasonable expectation of detecting material misstatements in the**[Insert details of statements being audited]** or accounting records (including those resulting from fraud, error or non-compliance with laws or regulations), but our examination should not be relied upon to disclose all such material misstatements as may exist. Due to the test nature and other inherent limitations of a financial audit there is an unavoidable risk that some material misstatement may remain undiscovered.

4.4.2Our work on internal control will not be sufficient to enable us to express any assurance on whether or not the **[Insert name of entity]** internal controls are effective. Our audit of the **[Insert details of statements being audited]** cannot be relied upon to draw to your attention all matters that may be relevant to your consideration as to whether or not the system of internal control is effective.

4.5 **Management representations**

As part of our audit process we will request from management written representations on matters material to the **[Insert details of statements being audited]** where other sufficient appropriate evidence cannot reasonably be expected to exist, and where management may have made certain oral representations (Letter of Representation).

4.6 **Reliance on third parties**

4.6.1 **Another auditor**

Where we place reliance on another auditor, we will consider how the work of the other auditor will affect the audit. We shall consider the professional competence of the other auditor in the context of this engagement and perform procedures to obtain sufficient evidence that the work of the other auditor is adequate for our purposes.

4.6.2 **Use of Experts**

Where we judge that it is appropriate to use the work of an expert we will:

- obtain sufficient appropriate audit evidence that such work is adequate for the purposes of the audit;
- evaluate the professional competence of the expert;
- evaluate the objectivity of the expert;
- ensure that the scope of the work of the expert is adequate for our purposes; and
- evaluate the appropriateness of the expert's work as audit evidence regarding the assertions being considered.

4.7 Communications

4.7.1 At the start of our audit, we may issue an Audit Plan, containing details of identified risks and planned financial audit work on the **[Insert name of entity]** for the coming year. This will detail where the audit team intends to make use of other auditors or experts.

4.8.2 At the end of each audit we will report formally to you on:

- Any significant weaknesses in, or observations on, the accounting and internal control system including areas of non compliance with applicable authorities;
- Errors identified in the course of the audit (unless deemed clearly trivial);
- Uncorrected misstatements;
- Expected modifications to the audit report; and
- Any other matters of interest.

5. CLIENT RESPONSIBILITIES

5.1 Our audit will be conducted on the basis that the Secretary **[Insert name of entity]** and those charged with governance acknowledge and understand that they have responsibility for:

(a) The preparation of financial statements that show a true and fair view in accordance with International Financial Reporting Standards;

(b) For such internal control as the Secretary**[Insert name of entity]** and those charged with governance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

(c) To provide us with:

- Access to all information of which the Secretary **[Insert name of entity]** and those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
- Additional information that we may request for the purpose of the audit; and

- Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

5.2 In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

6. **AUDIT ARRANGEMENTS**

6.1 **Access to Data and Personal Data**

As part of our audit work we may need access to personal data which the **[Insert name of entity]** holds. We will manage any personal data in accordance with the Statement on the Management of Personal Data at the OCAG (Annex 1).

6.2 **Health and Safety**

Members of the audit team will be in touch with relevant **[Insert name of entity]** to discuss practical arrangements and the timing of audit visits. However, we would appreciate your co-operation in relation to the provision of support for our employees covering health, safety and emergency arrangements applicable to your premises.

6.3.2 The **[Insert name of entity]** is also responsible for the controls over, and the security of their website. The examination of the controls over the maintenance and integrity of the **[Insert name of entity]**'s website is beyond the scope of our audit.

7. **OTHER MATTERS**

7.1 **Use of Report & Confidentiality**

Any formal report or other unpublished reports from us may not be provided to third parties. Such consent will be granted only on the basis that such reports are not prepared with the interests of anyone other than the **[Insert name of entity]** in mind and that we accept no duty or responsibility to any other party as concerns the reports.

7.2 **Quality of service**

We would like to provide you at all times with a high quality service to meet your needs. If at any time you would like to discuss with us how our service to you could be improved, please raise the matter immediately with me

ACCEPTANCE:

8.1 Once agreed, this arrangement will remain effective for future years unless it is terminated, amended or superseded. Should you wish to discuss any aspects of this before signing at the foot of this letter and returning a copy, please do not hesitate to contact me.

Yours Sincerely,

Date:

Director General
For and on behalf of
The Office of the Comptroller and Auditor General

ANNEX-A.2.2.1: Statement on the Management of Personal Data at the OCAG

1. The CAG and the OCAG have privileged and wide-ranging access to data and information to support the discharge of the audit function and ensure that the OCAG's reports to Parliament are factual, accurate and complete. This data relates both to public servants and individual citizens. We have a duty to respect this privileged access and to ensure that the personal information entrusted to us is safeguarded properly.

2. We take our obligations for data protection seriously. We have a body of data policies and IT standards, guidelines and procedures designed to ensure data protection. We keep our requests for personal data to the minimum necessary to complete our work and retain any personal information we obtain only for as long as we need it. We take appropriate measures to safeguard the integrity and confidentiality of data we hold from unauthorised access. All of our staff and contractors have an obligation to comply with our data protection policies.

3. Our definition of sensitive personal data includes data which, when held alone or in combination, could cause embarrassment, harm or financial loss to the data subject if disclosed to or tampered with by an unauthorised third party. We have separate arrangements in place for classified data.

4. To help you understand our commitment, we have developed a series of Personal Data Statements, which all our staffs subscribe to:

    - We will only request personal data for use in discharging our statutory and other audit functions and for lawful purposes. These requests are kept to the minimum necessary to carry out our work.

    - Our requests for personal data will be authorised by a senior employee. Each of our audits is led by a Director or Director General who is personally responsible for authorising any request for personal data in connection with that audit; maintaining records of the data held; ensuring it is securely and appropriately processed; ensuring it is securely and appropriately retained; and for certifying its destruction.

    - We will agree with you in advance how we will use, secure, destroy and account for the personal data you provide to us. We have a series of protocols which specify the measures for protecting personal data during transfer from the information provider, whilst we retain the information for audit purposes, for secure destruction of the data and for long term storage where this is required by professional standards.

    - We will notify you when we destroy personal data you have provided to us.

- We ensure our contractors operate suitable procedures for personal data protection before we pass such data to them. From time to time we contract with third parties who support us in discharging our responsibilities. Access to personal information will only be given to organisations which can show that they are capable of maintaining the standards defined in these statements.
- We audit our compliance with our data protection policies, in order to be assured that protection is in accordance with the terms of this Statement. These include checks on compliance carried out independently of the OCAG Directors responsible for the security of data on their audits.

Annex- B

UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

The purpose of this form is to document our understanding of the entity and its environment. Where appropriate, we should reference to supporting documents included in standing information in the file.

The questions within the form cover the areas where we typically need an understanding to be able to identify and assess risks of material misstatement or irregularity, and so plan and perform an effective audit.

This understanding is part of the standing information on the file. Each year we should perform appropriate Risk Assessment Procedures, as set out in the Overall Audit Strategy, to confirm or update our understanding. Where the director expects the standing information will remain current, we will perform procedures to determine that this information remains relevant. These procedures should consist of inquiry and, where appropriate, observation and inspection.

Where changes are needed to the standing information, we should obtain appropriate evidence for the changes and document what that evidence is. Depending upon what the update is, this may be through inquiry, examination of documentation, observation, or other means.

The areas where we should have an understanding of the entity and its environment are listed in the table below. Suggested points of focus that may be useful to consider for each element are available by reading the comments attached to each heading. These can be seen by opening the Reviewing Pane (using the Reviewing toolbar and Show -> Reviewing Pane). If the comments appear as "balloons" next to the text, these can be hidden using the Reviewing toolbar and Show-> Options, and uncheck "Use balloons in Print and Web layout".

If, having confirmed/updated our understanding of the entity and its environment, we have identified a potential risk of material misstatement/irregularity or information which will affect whether there is a risk, this should be discussed with the Engagement Manager and Engagement Director and clearly concluded upon.

Click on the underlined links to jump directly to the relevant factors.

(1) Relevant industry, regulatory, and other external factors (Ref: ISA 315 A17-A22, ISA 250 A7, ISA 540 A13-A15)
(2) The nature of the entity and its activities (Ref: ISA 315 para A23-A27)
(3) The entity's financial reporting and accounting policies (Ref: ISA 315 para A28)
(4) The entity's objectives and strategies, and related business risks (Ref: ISA 315 para A29-A35)
(5) The measurement and review of the entity's financial performance (Ref: ISA 315 para A36-A41)
(6) The nature and extent of the entity's related party relationships (Ref: ISA 550 para A11-A14)

CONCLUSION ON UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

(1) Relevant industry, regulatory, and other external factors (Ref: ISA 315 para A17-A22)

Relevant industry, regulatory and other external factors		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
a) What is the Authorising Legislation for the entity? What activities does it authorise?		
b) What are the Regulations issued under Authorising Legislation? How do they affect the entity's operations?		
c) What activities of the entity is there Parliamentary Authority for? Note: Though this directly relates to resource accounts, the principles apply to all central government bodies.		
d) What does the client need Treasury approval for? What does the client have delegated authority from Treasury for? Note: Though this directly relates to resource accounts, the principles apply to all central government bodies.		

e) Are there other elements of the legal and regulatory framework applicable to the entity which affects its operations? How does it comply with that framework?		
f) What is the nature of the entity's relationship with its sponsoring Department?		
g) What aspects of the Political Environment affect the entity's operations?		
h) What aspects of the Business Environment affect the entity's operations?		
i) How might future events affect the entity?		
j) Are there any other factors to consider? Consider any other external factors that may influence the business, operations or financial reporting of the client.		

(2) The nature of the entity and its operations (Ref: ISA 315 para A23-A27)

The purpose of understanding the nature of the entity and its operations is to enable an understanding of the classes of transactions, account balances and disclosures to be expected in the financial statements.

The nature of the entity.		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
a) What is the nature of the entity's operations? Where not obvious, consider indicating how significant audit areas relate to the entity's operations.		
b) What are the entity's ownership and governance structures?		
c) What types of investments is the entity making or planning to make (including investments in special-purpose entities)?		
d) How is the entity structured and how is it financed?		
e) What factors might affect whether the entity is a going concern?		

(3) The entity's financial reporting and accounting policies (Ref: ISA 315 para A28)

The entity's financial reporting and accounting policies		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
a) What financial reporting framework does the entity use for financial reporting? Are there any specific considerations that should be noted?		
b) Are there any historic judgements on accounting treatments to keep in view?		
c) How does the entity select and apply accounting policies? This should include estimation techniques used in applying accounting policies.		
d) What changes have there been to the entity's accounting policies in the period? What are the reasons for any changes?		
e) Are there any financial reporting standards and laws and regulations that are new to the entity? When and how will the entity adopt such requirements)?		
f) What are the principal accounting estimates in the entity's financial		

statements required by the financial reporting framework (including disclosures)?		
g) How do management identify the need for new accounting estimates (including disclosures)? How do management make those accounting estimates?		
h) Are the entity's accounting policies and estimation techniques used appropriate given: • the nature of its operations? • the requirements of the financial reporting framework? • accounting policies used elsewhere in government, or, where relevant, in relevant industries?		

(4) The entity's objectives and strategies, and related business risks (Ref: ISA 315 para A29-A35)

The entity's objectives and strategies and related business risks		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
What are the entity's objectives and strategies? What business risks are associated with the objectives and strategies and how might they impact the entity?		

(5) The measurement and review of the entity's financial performance (Ref: ISA 315 para A36-A41)

The measurement and review of the entity's financial performance		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
a) How is the entity's financial performance measured and reviewed?		
b) What are the entity's Financial and Performance Reporting Requirements?		
c) Are there any relevant external measures of financial performance available?		

(6) The nature and extent of the entity's related party relationships (Ref: ISA 550 para A11-A14)

(Note: It is usually effective to cross reference to standing documentation listing related parties.)

The nature and extent of the entity's related party relationships		
Including:	**Standing information** **(Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant** **(As set out in Overall Audit Strategy)**
a) What processes does the entity have in place to identify, account for, and disclose related party relationships and transactions?		
b) What is the authorisation and approval process for significant transactions and arrangements with related parties?		
c) How does the entity authorise and approve significant transactions and arrangements outside the normal course of business?		
d) What is the identity of the entity's related parties, including changes from the prior period? The client should supply a full listing of related parties each year.		
e) What is the nature of the relationships between the entity and these related parties?		

For on-going simple relationships this can be a link to the description in the financial statements. For complex, unusual or new relationships provide details as relevant.		
f) Has the entity entered into any transactions with these related parties during the period? If so, what is the nature and purpose of the transactions?		

Annex-B.1

Notes to assist Completion of Annex B

1) Relevant industry, regulatory, and other external factors (Ref: ISA 315 para A17-A22)

a) What is the Authorising Legislation for the entity? What activities does it authorise?

Authorising legislation includes primary sources of authority which govern the way in which an activity is performed, and the objectives pursued. Factors to consider may include:

- Acts of Parliament (express authorisation or prohibiting of specific activities, defined duties and limitations of Ministers and Officers, discretion permitted, authority to raise fees / collect receipts and rules thereof). Where expenditure is made (or revenue raised) under legislative authority, payments (or receipts) must comply with all relevant provisions. Strict compliance with the terms of enabling legislation is necessary for the regularity of income and expenditure.
- International Treaties and Agreements (the provisions of relevant treaties binding on the client, including subscription or other liabilities). There are specific requirements for notifying Parliament of proposals to create non-statutory liabilities, including liabilities to pay subscriptions or any other commitments, contingent or otherwise, under international treaties.

b) What are the Regulations issued under Authorising Legislation? How do they affect the entity's operations?

Delegated legislation takes a variety of forms, including rules, regulations and orders. Delegated legislation must always be intra vires, i.e. within the scope of the enabling power in the relevant Act. Factors to consider may include:

- Statutory Instruments such as detailed regulations for payment of grants or subsidies or performance targets set under statutory provisions
- Effect of delegated legislation on the client's financial statements
- The client's mechanisms for monitoring compliance with specific conditions attached to delegated legislation (own compliance or that of others)
- Ministerial Directions made under the authority of an Act of Parliament (detailed grant memorandum, compliance with a management statement, financial memorandum). Activities or transactions which are in breach of Ministerial direction under the authority of an Act of Parliament are irregular.

c) What activities of the entity is there Parliamentary Authority for?

Principles of Appropriation: A sum appropriated to a particular service cannot be used for another service, the appropriation may not be exceeded, and the sum is available only in the financial year for which it was appropriated. Consider the purposes for which Parliamentary provision is made as described in the ambit of the Estimate and the specific sums authorised for those purposes. Factors to consider may include:

- Regularity of expenditure in respect of ambit of services and correct financial year and the history of any previous irregularities. The ambit is the formal description of services to be financed from the Budget. Expenditure can, therefore, be legally incurred only on services which are covered by the ambit of the Budget.

The history of budgets being exceeded in the past. An Excess Spend (over budget) is taken very seriously since it represents a failure by a department/public body to keep its expenditure within the limits approved by Parliament.

d) What does the client need Ministry of Finance approval for? What does the client have delegated authority from the Ministry of Finance for?

The majority of Public Bodies require Ministry of Finance approval for all expenditure, including that authorised by statute. In practice delegated authority takes the form of a standing authorisation setting out the levels, programmes, objects and the time period. Consider the nature and extent of standing Ministry of Finance delegations and any requirements for the client to seek specific Treasury approval for particular expenditures or write-offs. Any expenditure which falls outside the department's delegated authority and which is not approved by Treasury is irregular. The same applies to any expenditure incurred in breach of a condition attached to a Ministry of Finance approval. Factors to consider may include:

- Ministry of Finance delegations applied to the client (powers of write-off, expenditure levels, authorities for letting major projects, authorities to participate in joint ventures, personnel policies, receipts and sources of finance). A delegation does not remove the obligation on Departments to submit any novel or contentious spending proposals to Ministry of Finance. The Accounting Officer is responsible for ensuring that prior Ministry of Finance approval is obtained in writing in all cases where required.
- Authorities governing personnel policies (remuneration, pensions)
- Authorities governing fees, charges and miscellaneous income
- Utilisation of savings on individual Budget lines and subheads to offset excess expenditure in other Appropriation areas, Ministry of Finance authorisation of virement requests).

e) Are there other elements of the legal and regulatory framework applicable to the entity which affects its operations? How does it comply with that framework?

For example anything set out in the authorising legislation that is applicable to the running of companies, Codes of Conduct, General Financial Rules.

f) What is the nature of the entity's relationship with its sponsors?

Consider the extent to which the client is subject to detailed oversight from its sponsoring ministry/department and the Ministry of Finance. Factors to consider may include:

- The approval of senior appointments to the client
- Sponsor department representation on the client's Board
- The sponsor department's role in setting business objectives and reviewing corporate and annual business plans
- Sponsoring department monitoring of client performance (consider the impact on potential results manipulation)
- Degree of sponsoring department influence on key client decisions
- Requirements for management control set out in the management statement / financial memorandum/or any other agreements between the audited entity and sponsor.

g) What aspects of the Political Environment affect the entity's operations?

In most areas of our work we are auditing on behalf of Parliament and through them the wider public. A high level of such interest may put pressure on the client and increase audit risk. It will also raise the profile of the audit. Consider any interest of the Government, Parliament, media and pressure groups in the client's activities and any specific factors that may influence the conduct of business or the reporting of its results. We should also consider whether the level of interest is likely to increase during the course of the audit, for example due to a forthcoming change in status or review of activities. Factors to consider may include:

- Government initiatives (quality improvements, major investments, changes to services, PFI, PPP, contracting out, Modernising Government)
- Public Accounts Committee interest
- Other Select Committee/Inquiry interest
- Funding from foreign donors (programme oversight, actions against the client, funding implications)
- Influence / interest of general press and specialist trade press
- Relationships with Ministry of Finance (Comprehensive Spending Review, Departmental Investment Strategy, Public Service Agreements).

h) What aspects of the Business Environment affect the entity's operations?

Financial statements are reports on the state of a business and its performance, whether the business is commercial or non-commercial. To understand, interpret and audit the financial statements we need to understand the business. Consider the client's business environment and those factors that may impact on the achievement of its objectives. Factors to consider may include:

- The entity's strategy or objectives and related business risks (ISA 315 para A30)
- Location (single or multi-site)
- Competitors and alternative suppliers
- External regulation or review of activities
- Relationship and circumstances of any suppliers or others upon which the client is reliant for the provision of service
- Dependence upon labour (skilled requirements, union activity)
- Method of funding
- Reliance upon fee and income generation
- Sensitivity of activities and results to general external economic factors (inflation, exchange and interest rates, unemployment).

i) How might future events affect the entity?

Consider any planned or potential future events, including changes in legislation, new programmes / services, known developments and changes in technology that may affect the client. Factors to consider may include:

- Proposals to change programmes and services administered by the client. Change of funding arrangements
- Proposals to reorganise the client in terms of geographical location, structure, early retirement and redundancy programmes
- New legislation (new Regulations and Directives)
- Major changes in technological and operational methods (this could include a move to the provision of on-line services to the public and the adoption of e-Procurement)
- Structural or business model changes.

j) Are there any other factors to consider?

Consider any other external factors that may influence the business, operations or financial reporting of the client.

(2) The nature of the entity and its operations (Ref: ISA 315 para A23-A27)

a) **What is the nature of the entity's operations?**

Where not obvious, consider indicating how significant audit areas relate to the entity's operations.

b) **What are the entity's ownership and governance structures?**
c) **What types of investments is the entity making or planning to make (including investments in special-purpose entities)?**
d) **How is the entity structured and how is it financed?**
e) **What factors might affect whether the entity is a going concern?**

Consider factors which could impact on our evaluation of the entity's going concern assessment. Factors to consider may include:

- whether the management and those charged with governance have performed a preliminary assessment of the entity's ability to continue as a going concern
- whether there are events or conditions that individually or collectively may cast significant doubt upon the entity's ability to continue as a going concern
- management's plans to address going concern issues.

(3)The entity's financial reporting and accounting policies (Ref: ISA 315 para A28)

This section will only be relevant to entities or activities (e.g. fund management) of an entity audited that have a financial reporting framework. It might not be relevant to all compliance audits undertaken.

(a) What financial reporting framework does the entity use for financial reporting? Are there any specific considerations that should be noted?

The financial reporting frameworks that could be relevant to Bangladesh include those for the Finance Accounts, Appropriation Accounts for individual departments, Financial Statements required under the terms of Donor Funding Agreements such as PEDP 3, Frameworks required for reporting Fund Management, Management Reports prepared by Chief Accounts Officers of Ministries, Project reports submitted by Project Directors and BAS compliant Financial Statements that are required to be prepared by Government Owned Limited Companies.

(b) Are there any historic judgements on accounting treatments to keep in view?

For example, a judgement over which standard applies to a particular class of transactions, or over the appropriate presentation of a recurring transaction stream.

This will only be relevant for audits of financial statements that are prepared under a recognised framework like International Standards of Accounting [Note that the pilot audits of Government owned Companies carried out under Round 2 revealed that the Financial Accounts audited by external firms of Chartered Accountants did not comply fully with International Accounting Standards despite their having been given a clean audit opinion].

(c) How does the entity select and apply accounting policies?

Points to consider include:

- the methods the entity uses to account for significant and unusual transactions
- whether there is an established process for selecting and approving accounting policies and estimation techniques
- the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus. This should include estimation techniques used in applying accounting policies.

See comments on 3 (b) above. Only applicable for audits of financial statements prepared under a recognised framework like International Accounting Standards.

(d) What changes have there been to the entity's accounting policies in the period? What are the reasons for any changes?

See comments on 3 (b) and 3 (c) above.

(e) Are there any financial reporting standards and laws and regulations that are new to the entity? When and how will the entity adopt such requirements)?

For example changes in donor reporting requirements or changes to the required format for appropriation accounts.

(f) What are the principal accounting estimates in the entity's financial statements required by the financial reporting framework (including disclosures)?

For example, provisions, revaluations and impairment estimates [Will only be applicable for accounts prepared under a recognised framework like IAS].

(g) How do management identify the need for new accounting estimates (including disclosures)? How do management make those accounting estimates?

Consider:

- the method, including models, used in making accounting estimates
- relevant controls
- whether management uses experts

- the assumptions used
- changes in circumstances affecting accounting estimates
- the extent of uncertainty in estimates

Will only be applicable for accounts prepared under a recognised framework like IAS.

(h) Are the entity's accounting policies and estimation techniques used appropriate given?

- the nature of its operations?
- the requirements of the financial reporting framework?
- accounting policies used elsewhere in government, or, where relevant, in relevant industries?

Will only be applicable for accounts prepared under a recognised framework like IAS.

(4) The entity's objectives and strategies, and related business risks (Ref: ISA 315 A29-A35)

What are the entity's objectives and strategies?

What business risks are associated with the objectives and strategies and how might they impact the entity?

Points to consider include:

- Industry developments (a potential related business risk might be, for example, that the entity does not have the personnel or expertise to deal with the changes in the industry)
- New products and services (a potential related business risk might be, for example, that there are exposures to new types of liabilities or regulations)
- Expansion of the business (a potential related business risk might be, for example, that the demand has not been accurately estimated)
- New accounting requirements (a potential related business risk might be, for example, incomplete or improper implementation, or increased costs)
- Regulatory requirements (a potential related business risk might be, for example, that there is increased legal exposure)
- Current and prospective financing requirements (a potential related business risk might be, for example, the loss of financing due to the entity's inability to meet requirements)
- Use of IT (a potential related business risk might be, for example, that systems and processes are incompatible)

- The effects of implementing a strategy, particularly any effects that will lead to new accounting requirements (a potential related business risk might be, for example, incomplete or improper implementation.

*** It is unlikely that any of the entities audited in Bangladesh would have a formal risk management policy or risk registers, but they should be encouraged to do so. The bullets above can act as a prompt for the audit teams to identify risks for the Significant Risk Testing Plan in the meantime.**

(5) The measurement and review of the entity's financial performance (Ref: ISA 315 para A36-A41)

a) How is the entity's financial performance measured and reviewed?

This section will only be relevant to entities or activities of an entity audited that have a financial reporting framework. It might not be relevant to all compliance audits undertaken.

Points to consider include:

- key performance indicators (financial and non-financial)
- key ratios, trends and operating statistics
- period-on-period financial performance analyses
- budgets, forecasts, variance analyses, segment information and divisional departmental or other level performance reports
- employee performance measures and incentive compensation policies
- comparison of the entity's performance with that of others

Unlikely to be relevant within the Bangladesh Accounting Framework apart from any variances against budgets reported to the Boards of entities audited.

(6) The nature and extent of the entity's related party relationships (Ref: ISA 550 para A11-A14)

Disclosure requirements will only be applicable if the Accounting Framework applicable to the entity being audited requires it.

a) What processes does the entity have in place to identify, account for, and disclose related party relationships and transactions?

Examples of related party relationships include:

- sponsoring bodies / departments
- subsidiary bodies
- other public sector bodies
- defined benefit pension schemes for employees

- board members / trustees
- key management staff
- for departments, their Ministers
- the families and connected businesses of each of the above.

b) What is the authorisation and approval process for significant transactions and arrangements with related parties?

c) How does the entity authorise and approve significant transactions and arrangements outside the normal course of business?

d) What is the identity of the entity's related parties, including changes from the prior period? The client should supply a full listing of related parties each year?

e) What is the nature of the relationships between the entity and these related parties? For on-going simple relationships this can be a link to the description in the financial statements. For complex, unusual or new relationships, provide details as relevant.

f) Has the entity entered into any transactions with these related parties during the period? If so, what is the nature and purpose of the transactions?

None of the Entities audited under the Government Framework are likely to have procedures for identifying related party transactions. However complying with the relevant procedures are part of the ISSAI requirements. Also, this is a key aspect of fraud prevention for example in relation to the awarding of large contracts.

Annex-C

UNDERSTANDING THE ENTITY'S INTERNAL CONTROL

We should confirm/update our understanding each year as part of our risk assessment procedures. The purpose of this form is to summarise our understanding of the entity's internal control. This form should:

- document our understanding of the overall control environment;
- link to our systems notes of control cycles; and
- link to where we have evaluated the design and implementation of controls (or, if this will be done later in the audit, where this will be documented).

Where appropriate, we should reference to supporting documents included in the file.

This understanding is part of the standing information on the file. Each year we should perform appropriate Risk Assessment Procedures, as set out in the Overall Audit Strategy, to confirm or update our understanding.

Where the director expects the standing information will remain current, we will perform procedures to determine that this information remains relevant. These procedures should consist of inquiry and, where appropriate, observation and inspection.

Where we plan to evaluate the design and implementation of a control, we will do so each year, which will involve evaluating:

- the design of a control requires a team to assess whether, if it operates as designed, it would reliably prevent or detect and correct material misstatement or irregularity.
- the implementation of a control requires a team to obtain evidence that it is implemented as designed (by walking through the relevant process, sighting evidence of the operation of a control, observation of the operation of the control, or other audit evidence).

Where changes are needed to the standing information, we should obtain appropriate evidence for the changes and document what that evidence is. Depending upon what the update is, this may be through inquiry, examination of documentation, observation, or other means.

The areas where we should have an understanding of the entity's internal control are listed in the table below. Suggested points of focus that may be useful to consider for each element are available by reading the comments attached to each heading. These can be seen by opening the Reviewing Pane (using the Reviewing toolbar and Show -> Reviewing Pane). If the comments appear as "balloons" next to the text, these can be hidden using the Reviewing toolbar and Show-> Options, and uncheck "Use balloons in Print and Web layout".

If, having confirmed/updated our understanding of the entity's internal control and its environment, we have identified a potential risk of material misstatement/irregularity or information which will affect whether there is a risk, this should be discussed with the Engagement Manager and Engagement Director and clearly concluded upon.

Click on the underlined links to jump directly to the relevant factors.

1) Control Environment (Ref: ISA 315 para A69-A78)
2) The entity's risk assessment process (Ref: ISA 315 para A79-A80)
3) Monitoring of controls (Ref: ISA 315 para A98-104)
4) Business controls (Ref: ISA 315 para A81-A87)
5) The information system (Ref: ISA 315 para A81-A85) and, if considered necessary: Annex A – Access Security Annex B – Change Management
6) Communication (Ref: ISA 315 para A86-A87)
7) Controls relevant to the audit (Ref: Para para A66-A68, A88-97)

Click on the underlined links to jump directly to the relevant factors.

1) Control Environment (Ref: ISA 315 para A69-A78)
2) The entity's risk assessment process (Ref: ISA 315 para A79-A80)
3) Monitoring of controls (Ref: ISA 315 para A98-104)
4) Business controls (Ref: ISA 315 para A81-A87)
5) The information system (Ref: ISA 315 para A81-A85) and, if considered necessary: Annex A – Access Security Annex B – Change Management
6) Communication (Ref: ISA 315 para A86-A87)
7) Controls relevant to the audit (Ref: Para para A66-A68, A88-97)

Control environment		
Including:	**Standing information (Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)**
d) How does the entity's organisational structure and assignment of authority and responsibility contribute to maintaining an appropriate control environment?		
e) How do the entity's Human Resources policies and procedures contribute to maintaining an appropriate control environment?		
f) What impact do any other relevant factors have upon the effectiveness of the control environment?		

2) The entity's risk assessment process (Ref: ISA 315 para A79-A80)

Public sector bodies should have a risk assessment process, which should be appropriate for the size and complexity of the entity. The risk assessment process is involved in:

(a) Identifying business risks relevant to financial reporting objectives;

(b) Estimating the significance of the risks;

(c) Assessing the likelihood of their occurrence; and

(d) Deciding about actions to address those risks.

The entity's risk assessment process		
Including:	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
a) Does management have an effective Risk Assessment Process?		
b) Does management use the Risk Assessment Process to effectively identify and respond to risks of fraud or irregularity?		
c) What are the results of management's Risk Assessment Process? Cross-reference to a copy of the results of management's process. Read and summarise any results of the client's risk assessment process that indicate potential risks of material misstatement or irregularity.		

3) Monitoring of controls （Ref: ISA 315 A98-104）

Public sector bodies should have a risk assessment process, which should be appropriate for the size and complexity of the entity. The risk assessment process is involved in:

(a) identifying business risks relevant to financial reporting objectives;

(b) estimating the significance of the risks;

(c) assessing the likelihood of their occurrence; and

(d) deciding about actions to address those risks.

Monitoring of controls		
Including:	**Standing information (Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)**
a) How does management monitor the effectiveness of the entity's internal control? What sources of information about the operation of controls are used in monitoring and how reliable are they?		
b) How reliable is the entity's Overall Financial Reporting and Budgetary Control?		
c) How effective is Internal Audit as part of the entity's		

Monitoring of controls		
Including:	**Standing information (Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)**
monitoring of controls?		
d) What impact do any other relevant factors have upon the entity's monitoring of controls?		

4) Business controls (Ref: ISA 315 para A81-A87)

The standing information in the file should include systems notes for each class of transactions in the entity's operations that are significant to the financial statements and for monitoring controls. The system notes should include:

- the procedures, within both information technology (IT) and manual systems, by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements. This should include how regularity is ensured;
- the related accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions. This includes the correction of incorrect information and how information is transferred to the general ledger. The records may be in either manual or electronic form; and
- how the information system captures events and conditions, other than transactions, that are significant to the financial statements.

System notes should clearly set out the flow of information within a business cycle, the IT systems involved, and where control activities and data interfaces take place (including controls over regularity). This can often be effectively documented using a system-flow diagram. The client or their internal audit team may have pre-prepared systems diagrams.
In addition to system notes on business cycles, our documentation should set out the financial reporting process used to prepare the entity's financial statements, including significant accounting estimates and disclosures, and the controls surrounding journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments.

Control cycle (Amend as appropriate to the entity)	Link to systems note (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
Receipts		
Payments		
Cash		

5) The information system （Ref: ISA 315 para A81-A85）

We should have sufficient understanding of the entity's information systems and their interaction with business controls (including controls over regularity) to be able to:

- identify any related risks of material misstatement or irregularity;
- identify where business controls are dependent upon general IT controls; and
- plan an effective and efficient audit.

Completing this section of the form

This section of the form documents our general understanding of the entity's information systems. Where appropriate, teams should link to detailed documentation of general IT controls held as standing information in the file. If the client has a document which sets out how they comply with the GSI security requirements, this may be an appropriate form of documentation (but this does not provide assurance that IT controls have been implemented or are operating effectively).

Based upon our general understanding we should identify whether there are any IT related risks or we will need to test general IT controls. This assessment can be performed in the IT Scope Assessment form.

We should complete Annex A of this form if we plan to rely on controls dependent upon general IT controls, or if the Engagement Director considers appropriate due to the complexity and significant of the entity's IT environment (as set out in the Overall Audit Strategy).

We should complete Annex B of this form if there have been significant changes in the IT system in the year, or if the Engagement Director considers appropriate due to the complexity and significant of the entity's IT environment (as set out in the Overall Audit Strategy).

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
What is/are the entity's IT system(s) involved in financial reporting?		
To what extent does the entity use the automated controls and checks within the IT system?		
How is the entity's IT system managed? What is the in-house IT team's structure/what is the structure of the relationship with outsourced suppliers?		
Is there any internal or external assurance over the operation of the IT system (e.g. internal audit, or attack and penetration testing)?		
Is there an IT strategy, how is it set, and how does it align to the business strategy?		

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
Is an IT Risk Assessment performed? What are the findings of the risk assessment?		
Data centre and network operations: If the entity uses data centres or networks in financial reporting, how is appropriate security maintained over the data?		
Access Security: What is the high level approach to systems security, including physical security of servers? *Where we consider we need to perform work on general IT controls per the IT scope assessment form, please complete Annex A.*		
Change management: How does the entity manage changes to IT systems involved in financial reporting		

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
or in controls over regularity of transactions?		
Have there been significant changes to the information systems environment during the year? *If there have been significant changes, please complete Annex B.*		
Other general aspects of the IT environment relevant to the audit		

Complete the IT Scope Assessment form based upon this understanding and, if necessary, complete Annex A and/or Annex B.

6) Communication (Ref: ISA 315 para A86-87)

Communication		
Including:	**Standing information (Update as required based on Risk Assessment Procedures performed)**	**Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)**
a) How does the entity communicate financial reporting matters internally?		
b) How does the entity communicate to employees policies on business practices and ethical behaviour?		
c) How does the entity communicate financial reporting matters externally?		

(7) Controls relevant to the audit （Ref: ISA 315 para A66-A68, A88-97）

We are required to evaluate the design and implementation of controls relevant to the audit in order to develop a sufficient understanding to plan and perform our audit, including, where relevant, IT controls. Depending on the timing of planning and of when these controls operate, we may perform this evaluation at the planning stage or later in our audit.

Where we plan to evaluate the design and implementation of a control, we will do so each year, which will involve evaluating:

- the design of a control requires a team to assess whether, if it operates as designed, it would reliably prevent or detect and correct material misstatement or irregularity.
- the implementation of a control requires a team to obtain evidence that it is implemented as designed (by walking through the relevant process, sighting evidence of the operation of a control, observation of the operation of the control, or other audit evidence).

Link in the table below to where our work on the evaluation of the design and implementation of controls has been performed.

Nature of control	Link to summary of D&I work	Issues relevant to D&I of controls not already noted above (Update by exception)
Controls that address Significant Risks （including where we plan to test their operating effectiveness）		
Other business cycle controls where we plan to test the operating effectiveness of controls （including application controls） （including where we need to test controls because we consider we cannot get sufficient assurance from only performing substantive testing）		
General IT controls where we plan to test their operating effectiveness （The IT scope assessor indicates whether we need to do so）		

Nature of control	Link to summary of D&I work	Issues relevant to D&I of controls not already noted above (Update by exception)
Month and year-end close process		
Accounting policies and financial statement production		
Monitoring		
Journals		
Overall regularity controls		
Other controls requiring Design & Implementation work[7] per the Overall Audit Strategy (provide details)		

[7] work to confirm the control is designed properly and implemented in a way that makes it auditable (i.e. there is evidence of its operation)

Annex C.1.A – Access Security

This annex should be completed if we plan to rely on controls dependent upon general IT controls, or if the Engagement Director considers appropriate due to the complexity and significance of the entity's IT environment (as set out in the Overall Audit Strategy).

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
What is the high level approach to systems security including physical security of servers？		
Has the entity achieved any IT Quality standard accreditation？		
What is the policy regarding passwords？		
What are the policies regarding user profiles and access？		
How are joiners' access privileges set？ What happens to leavers' access privileges？ （When staffs leave, what is the process for disabling their accounts and access privileges, and how long does it take？）		
How are administrator rights		

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
controlled？		
What Physical Access mechanisms are in place？		
How are remote third party systems accesses，including Electronic Data Interchange transactions）controlled？		
How is the Firewall used and controlled？		

Annex C.1. B - Change management

This annex should be completed if there have been significant changes in the IT system in the year, or if the concerned Director considers it appropriate due to the complexity and significant of the entity's IT environment (as set out in the Overall Audit Strategy).

This includes programme changes, system software acquisition, change and maintenance and application system acquisition, development and maintenance.

Issue	Standing information (Update as required based on Risk Assessment Procedures performed)	Description of Risk Assessment Procedures performed in current year to determine whether Standing Information remains relevant (As set out in Overall Audit Strategy)
Is there an Overall Development Approach to IT systems?		
How do projects get approved?		
Is there a separate development environment?		
How are new systems accredited?		
How are new systems tested before being placed in the live environment?		
How are systems / changes migrated into the live environment?		

Annex-D

IT SCOPE ASSESSMENT

Summarise below the outcome of identification of IT risks and identification of controls dependent upon IT.

Consider both impact and likelihood in considering whether there are risks of material misstatement or irregularity.

	Summary Question	Answer	Audit response	Link	Comments
	Identification of IT risks				
1	Have any potential risks of material misstatement or irregularity relating to IT been identified?				
2	Do any of these represent Pervasive Risks?				
3	Do any of these represent Specific Risks?				
4	Do any of these require other testing to be performed (i.e. there is a risk of material misstatement or irregularity)?				
5	Do any of these represent Risk Factors, which should be kept in view through the audit but do not require any additional specific audit response?				
	Identification of controls dependent upon IT				
6	Do we plan to obtain assurance from the operating effectiveness of controls (e.g. controls over regularity of grants, payroll controls, expenditure controls)?				

7	Are any of the controls which we plan to rely on dependent upon general IT controls （including operational systems）（e.g. application controls calculating grant payments in line with scheme rules）?				

Based upon our understanding of the entity's information systems, consider whether there are any Significant Risks, other issues requiring a response or Risk Factors relating to IT.

(Expand for examples of risks)

Consider both impact and likelihood in considering whether there are risks of material misstatement or irregularity.

	Question (expand grouped cells for examples)	**Answer**		**Does this represent a Significant Risk, require other testing, or represent a Risk Factor which does not require any additional specific audit response?**	**Explanation of classification of whether a risk / other comments (Link if transferred to AASF)**		
	IT system and staffing						
1	Have there been significant new IT systems related to financial reporting or regularity of transactions in the year?						
2	Have there been other significant changes in the IT environment in the year?						
3	Are there any inconsistencies between the entity's IT strategy and its business strategies?						

4	Is there an insufficient level of staffing of the IT department with sufficient skills to mitigate the risks to the business?						
5	Have there been changes in key IT personnel in the period?						
6	Is the management of the IT system outsourced? (Note – even if this does not represent a Significant Risk, this may affect our audit approach)						
	Operation of IT system						
7	From our understanding of the information systems, are there any indications that the financial accounting systems (or systems involved in the regularity of transactions) are inaccurately processing data (in particular are there IT-related instances of past misstatements, irregular transactions, history of errors or a significant amount of adjustments at period end?)?						
8	From our understanding of controls around journals, are there inappropriate access controls over entries to the financial accounting system or systems involved in regularity of transactions?						

9	From our understanding of the information systems, is there inappropriate segregation of duties within the financial reporting system, systems involved in the regularity of transactions or the IT system?						
10	Are management aware of any breakdowns in the operation of IT controls around the financial accounting system or systems involved in the regularity of transactions?						
	Application controls						
11	Are there IT application controls which do not appear to be appropriately designed or implemented (without mitigating controls)?						
12	Are there changing circumstances for the entity which may require a control response outside the scope of existing automated controls?						
	Other						
13	Are spreadsheets used to generate figures for inclusion in the financial statements, or in ensuring the regularity of transactions, (without appropriate						

	controls to check the design of the spreadsheets and control changes to them)?						
14	Are there any other factors that indicate one or more actual or potential risks related to IT controls or environment?						

Based upon our understanding of the entity's internal control and in particular of the entity's information systems, consider whether any of the controls we plan to rely on are dependent upon general IT controls.

Expand for examples of issues.

Expand to comment by transaction cycle or other disaggregated basis.

	Question	Answer	Impact on audit	Comments on transaction cycles / audit areas where we plan to rely on controls Comments/ details of assessment
	Automated controls			
1	Are any of the controls which we plan to rely on automated controls (e.g. controls which directly affect or control the processing of a transaction or event through the operation of controls within application software, automated controls over regularity of transactions)?			
	Manual controls			
	The purpose of considering how general IT controls support manual controls is to identify whether the effective operation of the manual control is			

	dependent upon general IT controls. If a general IT control needs to operate effectively to enable a manual control to work, we would need to test the general IT control as well.			
2	If the information systems processed data incorrectly, would this impact upon the operation of any of the controls that we plan to rely upon?			
3	If access controls to the information systems did not operate effectively, could inappropriate access to the system prevent the effective operation of any of the controls that we plan to rely on?			
4	If the information system did not enforce segregation of duties, would this prevent the effective operation of any of the controls that we plan to rely on?			
5	If changes have been made to the information systems in the year, could inappropriate changes or unforeseen effects of changes prevent the effective operation of any of the controls that we plan to rely on?			

Annex-E

Fraud Risk Assessment

Introduction

The Fraud Risk Assessment form is designed to assist auditors in the evaluation of the potential risks of fraud in arriving at an assessment of the risk of material misstatement due to fraud.

The Engagement Team should evaluate whether the information obtained from the other risk assessment procedures and related activities performed indicates that one or more factors indicating potential risks are present. Whilst these factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and, therefore, may indicate risks of material misstatement due to fraud. (ISA 240 para 24)

The Engagement Team should identify and assess the risk of material misstatement due to fraud at the financial statement level and at the assertion level for classes of transactions, account balances and disclosures. (ISA 240 para 25)

Identification of potential risks of fraud

Three conditions are generally present when fraud exists:

- an incentive or pressure to commit fraud;
- a perceived opportunity to commit fraud; and
- an ability to rationalise the fraudulent actions.

In assessing potential risks of fraud the Engagement Team should have mind to the existence of these conditions.

ISA 240 provides examples of factors to consider in assessing the risk of material misstatement due to fraud. Although these cover a broad range of circumstances, they are only examples and other indicators may exist.

Use of this form

This form consists of four tabs:

- "Financial Reporting" which considers the factors listed in the ISA which may give rise to a significant risk of material misstatement arising from fraudulent financial reporting;

- "Misappropriation" which considers the factors listed in the ISA which may give rise to a significant risk of material misstatement arising from misappropriation of assets;
- "Misappropriation External" which considers possible indicators of risks of misappropriation by individuals not employed by the entity which may give rise to a risk of irregularity (while not being a fraud risk under ISA 240) arising from misappropriation of assets; and
- "Summary of assessment" which draws together the results of our consideration of potential risks and documents our conclusion as to whether the results of that consideration indicate a risk of material misstatement arising from fraud (which would be a Significant Risk) or are otherwise indicative of a risk of material irregularity.

Each tab contains a series of high level questions addressing the presence of indicators of a risk of material misstatement due to fraud. Where relevant detailed indicators to consider when assessing whether the factor is present are listed. The questions and indicators are drawn from the annexes to ISA 240. Whilst these cover a broad range of circumstances they are only examples and teams should consider whether other potential risks exist as indicated by the risk assessment procedures performed.

Engagement Teams should consider whether, as a result of the evidence obtained from the performance of risk assessment procedures, they have any evidence to indicate that there are indications of a risk of material misstatement.

In assessing the indicators identified, the Engagement Team should consider whether individually or in aggregate they indicate a risk of material misstatement due to fraud, taking account of existence of the conditions generally present when fraud exists.

If any risks of material misstatement are identified, they should be classified as a Pervasive or Specific Risk in accordance with para 27 of ISA 240 and the engagement teams should plan and perform appropriate responses as per any other Significant Risk.

If any risks of material irregularity are identified, we should consider whether they represent a Significant Risk. We should plan and perform responses as per a Significant Risk or other risk of material misstatement as appropriate.

Annex-E.1

Fraud Risk Assessment

Summarise below the considerations of potential risks identified through our risk assessment procedures.
Consider both impact and likelihood in considering whether there are risks of material misstatement or irregularity.

Summary Questions	Potential risks identified for the entity	Do these individually or in aggregate indicate – a risk of material misstatement (which, as a fraud risk, is a Significant Risk); or – or a risk of material irregularity (including Significant Risks)?	Is this a Pervasive or a Specific Risk?	Response	Comments (including any explanation required of why we consider potential risks identified do not give rise to risks of material misstatement)
Fraudulent financial reporting					
Do incentives or pressures exist which increase the risk of fraudulent financial reporting?					
Does the existence of opportunity indicate an increased risk of fraudulent financial reporting?					

Do the attitudes of staff, or other conditions, exist which would enable staff to rationalize their actions, indicate an increase risk of fraudulent financial reporting?					
Is there a risk of material misstatement relating to fraudulent financial reporting?					
Misappropriation of assets by employees or management					
Do incentives or pressures exist which increase the risk of fraudulent misappropriation of assets?					
Does the existence of opportunity indicate an increased risk of fraudulent misappropriation of assets?					
Do the attitudes of staff, or do conditions exist which would enable staff to rationalize their actions, indicate an increased risk of fraudulent misappropriation of assets?					
Is there a risk of material misstatement relating to misappropriation of assets?					
As a result of the work performed considering potential risks relating to fraudulent financial reporting or misappropriation of assets by employees or management, have we identified any risks of material irregularity, including Significant Risks, to be addressed through the audit?*					

Misappropriation of assets by individuals or groups external to the organisation					
Does the existence of opportunity indicate an increased risk of misappropriation of assets by individuals or groups external to the entity?					
Do incentives exist which increase the risk of misappropriation of assets by individuals or groups external to the entity?					
Is there a history or expectation of misappropriation of assets by individuals or groups external to the entity?					
As a result of the work performed considering potential risk relating to misappropriation of assets by individuals or groups external to the entity, have we identified any risks of material irregularity, including Significant Risks, to be addressed through the audit?					
* misappropriation of assets is irregular and risk of material misappropriation of assets due to fraud is considered, which places an emphasis on misappropriation by management or employees.					

Consider potential risks relating to misstatements arising from fraudulent financial reporting.

Question (expand grouped cells for examples)	**Indicators**	**Answer**	**Potential risk(s) identified**
Do incentives or pressures exist which increase the risk of fraudulent financial reporting?			
Is financial stability or profitability is threatened by economic, industry, or entity operating conditions?	- High vulnerability to rapid changes, such as changes in technology, product obsolescence, or interest rates. - New accounting, statutory, or regulatory requirements. - High degree of competition or market saturation, accompanied by declining margins. Significant declines in customer demand and increasing business failures in either the industry or overall economy. - Operating losses making the threat of bankruptcy, foreclosure, or hostile takeover imminent. - Recurring negative cash flows from operations or an inability to generate cash flows from operations while reporting earnings and earnings growth.		

	- Rapid growth or unusual profitability especially compared to that of other companies in the same industry.		
Do excessive pressures exist for management to meet the requirements or expectations of third parties?	- Profitability or trend level expectations of investment analysts, institutional investors, significant creditors, or other external parties (particularly expectations that are unduly aggressive or unrealistic), including expectations created by management in, for example, overly optimistic press releases or annual report messages. - Need to obtain additional debt or equity financing to stay competitive – including financing of major research and development or capital expenditures. - Marginal ability to meet exchange listing requirements or debt repayment or other debt covenant requirements. -Perceived or real adverse effects of reporting poor financial results on significant pending transactions, such as business combinations or contract awards.		

Does the information available indicate that the personal financial situation of management is threatened by the entity's financial performance?	- Significant financial interests in the entity. - Significant portions of their compensation (for example, bonuses, stock options, and earn-out arrangements) being contingent upon achieving aggressive targets for stock price, operating results, financial position, or cash flow. - Personal guarantees of debts of the entity.		
Is there excessive pressure on management or operating personnel to meet financial targets established (by sponsors), including sales or profitability incentive goals?			
Do other incentives or pressures exist?			
Does the existence of opportunity indicate an increased risk of fraudulent financial reporting?			
Do the attitudes of staff, or other conditions, exist which would enable staff to rationalize their actions, indicate an increase risk of fraudulent financial reporting?			

Consider potential risks relating to misstatements arising from misappropriation of assets by employees or management.

Question (expand grouped cells for examples)	**Answer**	**Potential risk(s) identified**
Do incentives or pressures exist which increase the risk of fraudulent misappropriation of assets?		
Does the existence of opportunity indicate an increased risk of fraudulent misappropriation of assets?		
Do the attitudes of staff, or do conditions exist which would enable staff to rationalize their actions, indicate an increase risk of fraudulent misappropriation of assets?		

Consider potential risks of irregularities arising from misappropriation of assets by individuals or groups external to the entity.

Question (expand grouped cells for examples)	**Indicators**	**Answer**	**Potential risk(s) identified**
Does the existence of opportunity indicate an increased risk of misappropriation of assets by individuals or groups external to the entity?			
Are we aware of any characteristics or circumstances that may increase the susceptibility of assets to misappropriation?	- Complex legislative framework or requirements including those covering taxes and benefits. - The entity administer a complex series of schemes or processes which could be subject to manipulation or misunderstanding.		
Is the internal control over designed to prevent or detect the misappropriation of assets inadequate?	- The entity's processing caseload has been subject to significant increase in the levels of business. - As part of the controls system the entity is required to operate a pre-screening or eligibility checks, e.g. credit referencing, Companies House checks, financial standing / track record enquiries. - Service delivery systems have been changed to facilitate improved service delivery speeds. - Functions performing control activities have been cut back, e.g. due to budget constraints.		
Are there other factors indicating that opportunities exist?			

Do incentives exist which increase the risk of misappropriation of assets by individuals or groups external to the entity?	- The entity is involved in delivering services or benefits directly to individuals who derive a personal benefit from it. - Entitlement to a benefit or credit scheme also provide the individual with passported entitlements to other benefits.		
Is there a history or expectation of misappropriation of assets by individuals or groups external to the entity?	- The entity's estimates of losses arising from external fraud are high or have increased. - The C&AG's audit opinion on regularity has been qualified in the past in respect of external fraud and misappropriation - There has been a substantial increase in caseload services or benefits delivered by the entity which is not consistent with changes in the external environment.		

Significant Risks Testing Plan (SRTP)

Introduction

The Significant Risks Testing Plan is intended as the key form of summarising the audit plan for addressing the Pervasive Risks and Specific Risks in the audit. The approach for other areas of the audit is summarised in the Audit Area Testing Plan. The aims of the Testing Plans are to provide a manageable means of viewing the overall audit approach and to facilitate discussion of the approach at the planning meeting.

The form also provides a method by which additional members of the audit team can view the overall audit approach resulting from the risk and controls assessment and to enable managers and directors to easily review the planned approach.

The form does not document the results of testing which will be documented in the Pervasive and Specific Risks folders in AMMS.

The form should be completed electronically if possible.

Format of the form and instructions on use

Auditors are required to first populate the Significant Risks Testing Plan with the Pervasive Risks and Specific Risks arrived at as part of the planning process.

On the Pervasive Risks sheet auditors should document what the Pervasive Risk is, any mitigating management controls, and the steps taken to address the risk.

On the Presumed Fraud Risks sheet auditors should document the responses to the risk of Management Override, and whether there is a risk of fraud in revenue recognition for the entity and related responses.

On the Specific Risks sheet auditors should document what the risk is, the audit area and assertion affected, any mitigating management controls, and the steps taken to address the risk.

The information included in this form should be consistent with the documentation of the approach in the Overall Audit Strategy (updated to reflect issues identified during the Risk Assessment Procedures)

Annex– F.1

risks identified	Controls mitigating the pervasive risks identified	Control design and implementation assessment		Summary of overall responses to Pervasive Risk (including controls tests and/or substantive procedures if appropriate)	
cells will expand to fit one line if se Alt+Enter to w line to start ame cell)		*(Adequate / Not adequate)*	Link		Link
ancial Reporting					

Annex F –1.1

No.	Description of the Specific Risk	Audit area(s) affected	Audit assertion(s) affected	planned extent of controls work (at minimum D&I)	Control design and implementation assessment		Planned to test operating effectiveness of controls	Controls test description and procedure summary / step reference		Is the control dependent upon general IT controls?	Control effectiveness assessment	Controls assurance	Substantive assurance	Substantive test to address the specific identified risks – procedure summary / step reference		Do the planned procedures provide all of the assurance needed over the relevant assertion(s) for the Audit Area(s)
	(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start		*Note – if more than one assertion affected, these will need to be typed in*		*(Adequate / Not adequate)*	Link	*(Yes / No)*	*(Controls should address each assertion if control assurance is to be taken over that assertion)*	Link	*(Yes / No)* *(include link)*	*(Effective / Not effective)*			*(Planned procedures should be tailored to address the risk itself and the assertion it relates to, rather than being general procedures.* *Procedures*	Link	(i.e. will more work be needed on the assertion for the Audit Area) (add comment as required)

	within the same cell)													may include CAATs or work to place reliance upon the work of management. Procedures should not consist solely of substantive analytical procedures unless controls assurance obtained)		
1																
2																
3																
4																
5																
6																

Presumed Fraud Risk	Considerations particular to the client	Controls mitigating the risk	Control design and implementation assessment		Planned responses (including those required by ISA 240, and any other overall responses, tests of control or substantive procedures considered appropriate)	
			(Adequate / Not adequate)	Link		Link
Revenue recognition						
ISA 240 has a rebuttable presumption of fraud in revenue recognition. Complete as applicable:						
The risk of fraud in revenue recognition for ***income*** has/has **not** been rebutted and has/has not been raised as a specific risk.						

Management override of controls. Note – this risk cannot be rebutted, and there are required responses in respect of journal entries, accounting estimates, and significant or unusual transactions. These responses should be tailored to the circumstances of the entity. If there are additional risks of management override of controls, these should also be reflected below or as Pervasive or Specific Risks						
Journal testing Para 32 of ISA 240 requires the engagement team to test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. In designing and performing audit procedures for such tests, the auditor shall: (i) Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments; (ii) Select journal entries and other adjustments made at the end of a reporting period; and						

(iii) Consider the need to test journal entries and other adjustments throughout the period.						
Bias in accounting estimates Para 32 of ISA 240 requires engagement teams to review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. In performing this review, the auditor shall: (i) Evaluate whether the judgements and decisions made by management in making the accounting estimates included in the financial statements, even if they are individually reasonable, indicate a possible bias on the part of the entity's management that may represent a risk of material misstatement due to fraud. If so, the auditor shall reevaluate the accounting estimates taken as a whole; and (ii) Perform a retrospective review of management judgements and assumptions related to significant accounting estimates reflected in the financial statements of the prior year. (Ref: ISA 240 Para A45-A47)						

Significant or unusual transactions Para 32 of ISA 240 requires for significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment and other information obtained during the audit, the auditor shall evaluate whether the business rationale (or the lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets. (Ref: ISA 240 Para A48)						

Assertions about classes of transactions and events for the period under audi

Completeness	C	All transactions and events that should have been recor have been recorded.
Occurrence	O	Transactions and events that have been recordedh occurred and pertain to the entity.
Accuracy	A	Amounts and other data relating to recorded transactions events have been recorded appropriately.
Cut Off	Cu	Transactions and events have been recorded in the cor accounting period.
Regularity	R	Financial transactions are in accordance with the legisla authorising them, regulations issued by a body with the po to do so under governing legislation, Parliamentary autho and HM Treasury authority.
Classification	Cl	Transactions and events have been recorded in the pro accounts.

Assertions about account balances at the period end

Completeness	C	All assets, liabilities and equity interests that should have been recorded have been recorded.
Existence	E	Assets, liabilities, and equity interests exist.
Valuation and allocation	V	Assets, liabilities and equity interest are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.
Rights and obligations	R&O	The entity holds or controls the rights to assets, and liabilities are the obligations of the entity.

Assertions about presentation and disclosure

Completeness	C	All disclosures that should have been included in the financial statements have been included
Occurrence	O	Disclosed events, transactions and other matters have occurred
Accuracy and Valuation	A&V	Financial and other information is disclosed fairly and at appropriate amounts
Rights and obligations	R&O	Disclosed events, transactions and other matters pertain to the entity
Classification and Understandability	Cl&U	Financial information is appropriately presented and described, and disclosures are clearly expressed

Audit Area Testing Plan

Introduction

The aims of the Audit Area Testing Plan is to provide a manageable means of viewing the audit approach for audit areas and to provide a means of documenting the sources of assurance.

The form also provides a method by which additional members of the audit team can view the planned audit approach and to enable managers and directors to easily review the planned approach.

The form does not document the results of testing, which should be recorded on the Audit Area Lead Schedule together with confirmation that the testing plan has been completed as planned, or that changes have been made to the plan.

If our evaluation of the design and implementation of controls we planned to rely on, or tests of the operating effectiveness of those controls, indicate that we cannot rely on them, this testing plan should be updated and changes made documented on the Lead Schedule.
The form can be used to satisfy the requirements of the Audit Area Testing Approach test in each audit area. The planned approach for each audit area should reflect the Overall Audit Strategy (e.g. whether to rely on controls and any other issues identified in the OAS). If any changes are made to the planned approach, this should be agreed with the Director and updated on the OAS. The planned Procedure Steps should reflect this Testing Plan.

Format of the form and instructions on use

Auditors are required to first populate the Testing Plan for Audit Areas with the Pervasive Risks and Specific Risks and audit areas arrived at as part of the planning process, and highlighted on Part 2 of the Understanding the Business Form and the Entity Level Management Controls Form.

The **"Financial Statements"** tab should be used to document planned tests to address risks that could affect any audit area or the financial statements as a whole, including related parties, overall regularity issues, going concern, or laws and regulations. Where these issues give rise to a Significant Risk, this should be documented on the Significant

Risk Testing Plan.

The **"Audit Areas"** tab(s) should be used to document the approach to testing each assertion for Audit Areas. Audit Areas should be identified at a sufficient level of granularity to enable us to plan our testing approach, and so should consist of items with a similar nature, risks and controls. A financial statement note item may be made up of several separate Audit Areas.

Auditors should indicate whether each audit area is significant or not, and the planned control approach.

If a Specific Risk has been identified affecting an assertion, auditors should indicate whether either:

- the Specific Risk will be extending the testing documented on this Testing Plan (e.g. performing substantive testing with an AF of 3.0, rather than 2.0); or
- the tests addressing the Specific Risk will be in addition to the testing documented on this Testing Plan

In either instance, auditors should cross-reference the link to the relevant Specific Risk on the Significant Risks Testing Plan.

The form indicates the required level of substantive assurance given the planned audit approach.

The final columns of the plan are the summarised substantive procedures that will be carried out in each audit area. The summary of procedures shows the procedures on assertions which are not Specific Risks: procedures to address Specific Risks are dealt with on the Audit Approach Summary Form. Hyperlinks should be used to indicate where additional information can be found.

Auditors can record any risk factors identified to keep in view during testing on the **"Risk Factors"** tab. These are either:

- risks of material misstatement or irregularity which are addressed through standard planned testing over the relevant assertions, and so do not require any additional specific audit response; or
- potential risks which have been assessed as not representing a risk of material misstatement/irregularity, and so do not require an audit response.

Annex–G.1

RISK FACTORS IDENTIFIED

Summarise below any risk factors identified in planning (i.e. either:

- risks of material misstatement or irregularity which are addressed through standard planned testing over the relevant assertions, and so do not require any additional specific audit response; or
- potential risks which have been assessed as not representing a risk of material misstatement/irregularity, and so do not require an audit response).

The below risk factors should be considered through the audit as part of maintaining an attitude of professional skepticism and, if necessary due to changes in circumstance or our understanding of the risk factors, additional procedures performed.

Risk factor	Pervasive / Audit area(s) and assertion(s) potentially affected	Comments on why considered only a risk factor	Procedures required (if any – typically not required, but may be performed to reassess whether a risk at year-end)

Annex- G.2

Audit Areas- Financial Statements

Area	Requirement	Test in Teammate	Are there any related Significant Risks?			Do we plan to rely on controls?	Other comments on planned procedures	
(Add others as required, e.g. Opening balances for initial audit engagements)				*Details*	*Link to SRTP*		*(By exception as required, e.g. where need to specify what is done beyond the standard procedures)*	
Trial balance	Confirm that the audited figures for last year's accounts have been correctly posted as the opening balances in the general ledger.	TB: Trial balance opening figures						
	Ensure that the Trial Balance has been correctly drawn from the General Ledger.	TB: General ledger to TB						
	Demonstrate that the audit area totals reconcile to the trial balance and or draft account.	TB: Reconciliation to audited figures						

Annex-G.3

Audit Areas- Income

Audit area	Value used in assessing significance of audit area	Significant or non–significant audit area	Audit assertion	Do we plan to rely on the operating effectiveness of controls?	Description of the control which addresses the assertion	Description of the planned work to evaluate the design and implementation of the control, AND the planned test of operating effectiveness if appropriately designed and implemented	Is the control dependent upon general IT controls?	ve any Specific Risks been identified for this assertion, and will they be addressed by this testing?	Planned inherent assurance	Planned controls assurance	Planned substantive assurance	Substantive tests description and procedure summary / step reference

(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start within the same cell.)	Income Type 1			
[Specify source – e.g. PY, budget, P9, draft accounts]				
(Significant / Non-Significant)				
	Occurrence	Completeness	Accuracy	Cut Off
(Evaluation of D&I for Specific Risks where we do not plan to test OE is on the SRTP)				
(Only required if we plan to test the operating effectiveness of the control)				
(Controls should address each assertion if control assurance is to be taken over the balance as a whole. Documentation should clearly state which assertions are covered by controls.)				
Link to planned controls work				
(Yes / No)				
Link to planned IT controls work				
Link to the related Specific Risk on the Significant Risks Testing Plan				
Where assertions are not covered by controls assurance (which is typically the case for classification), additional procedures will need to be set out herein.				
Link				

Classification	Regularity	Occurrence	Completeness	Accuracy	Cut Off	Classification
		Income Type 2				

Regularity	Occurrence	Completeness	Accuracy	Cut Off	Classification	Regularity
	Income Type 3					

Annex-G.4

Audit Areas-Expenditure

Audit area	*(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start within the same cell.)*	Expenditure
assessing significance of audit area	*[Specify source – e.g. PY, budget, P9, draft accounts]*	
non-significant audit area	*(Significant / Non-Significant)*	
Audit assertion		Occurrence
rely on the operating effectiveness of controls?	*(Evaluation of D&I for Specific Risks where we do not plan to test OE is on the SRTP)*	
which addresses the	*(Only required if we plan to test the operating effectiveness of the control)*	
implementation of the control, AND the planned test of operating effectiveness	*Link to planned controls work*	
	assertion if control assurance is to be taken over the balance as a whole. Documentation should clearly state which assertions are covered by controls.)	
Is the control dependent upon general IT controls?	*Link to planned IT controls work*	
	(Yes / No)	
identified for this assertion, and will they be addressed	*Link to the related Specific Risk on the Significant Risks Testing Plan*	
inherent assurance		
controls assurance		
substantive assurance		
Substantive tests description and procedure summary / step reference	*Where assertions are not covered by controls assurance (which is typically the case for classification), additional procedures will need to be set out herein.*	
	Link	

Completeness	Accuracy	Cut Off	Classification

Regularity	

Audit Areas-Payroll

Annex-G.5

Audit area	Value used in assessing significance of audit area	Significant or non-significant audit area	Audit assertion	Do we plan to rely on the operating effectiveness of controls?	Description of the control which addresses the assertion	Description of the planned work to evaluate the design and implementation of the control, AND the planned test of operating effectiveness if appropriately designed and implemented	Is the control dependent upon general IT controls?	Have any Specific Risks been identified for this assertion, and will they be addressed by this testing?			Planned inherent assurance	Planned controls assurance	Planned substantive assurance		Substantive tests description and procedure summary / step reference
(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start within the same cell.)	*[Specify source – e.g. PY, budget, P9, draft accounts]*	*(Significant / Non-Significant)*		*(Evaluation of D&I for Specific Risks where we do not plan to test OE is on the SRTP)*	*(Only required if we plan to test the operating effectiveness of the control)*	*(Controls should address each assertion if control assurance is to be taken over the balance as a whole. Documentation should clearly state which assertions are covered by controls.)*	*Link to planned controls work*	*(Yes / No)*	*Link to planned IT controls work*	*Link to the related Specific Risk on the Significant Risks Testing Plan*				*Where assertions are not covered by controls assurance (which is typically the case for classification), additional procedures will need to be set out herein.*	*Link*
Payroll			Occurrence												

Completeness	Accuracy	Cut Off	Classification	Regularity

	Link
Substantive tests description and procedure summary / step reference	*Where assertions are not covered by controls assurance (which is typically the case for classification), additional procedures will need to be set out herein.*
Planned substantive assurance	
Planned controls assurance	
Planned inherent assurance	
Have any Specific Risks been identified for this assertion, and will they be addressed by this testing?	*Link to the related Specific Risk on the Significant Risks Testing Plan*
Is the control dependent upon general IT controls?	*Link to planned IT controls work*
	(Yes / No)
Description of the planned work to evaluate the design and implementation of the control, AND the planned test of operating effectiveness if appropriately designed and implemented	*Link to planned controls work*
	(Controls should address each assertion if control assurance is to be taken over the balance as a whole. Documentation should clearly state which assertions are covered by controls.)
Description of the control which addresses the assertion	*(Only required if we plan to test the operating effectiveness of the control)*
Do we plan to rely on the operating effectiveness of controls?	*(Evaluation of D&I for Specific Risks where we do not plan to test OE is on the SRTP)*
Audit assertion	
Significant or non-significant audit area	*(Significant / Non-Significant)*
Value used in assessing significance of audit area	*[Specify source – e.g. PY, budget, P9, draft accounts]*
Audit area	*(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start within the same cell.)*

Existence	Rights and obligations	Completeness	Valuation and allocation	Existence
Receivables				Cash

Rights and obligations	Completeness	

Audit Areas-Accounts Payable

Audit area	Value used in assessing significance of audit area	Significant or non-significant audit area	Audit assertion	Do we plan to rely on the operating effectiveness of controls?	Description of the control which addresses the assertion	Description of the planned work to evaluate the design and implementation of the control, AND the planned test of operating effectiveness if appropriately designed and implemented	Is the control dependent upon general IT controls?		Have any Specific Risks been identified for this assertion, and will they be addressed by this testing?		Planned inherent assurance	Planned controls assurance	Planned substantive assurance	Substantive tests description and procedure summary / step reference	
(Note – cells will automatically expand to fit more than one line if required. Use Alt+Enter to force a new line to start within the same cell.)	[Specify source – e.g. PY, budget, P9, draft accounts]	(Significant / Non-Significant)		(Evaluation of D&I for Specific Risks where we do not plan to test OE is on the SRTP)	(Only required if we plan to test the operating effectiveness of the control)	(Controls should address each assertion if control assurance is to be taken over the balance as a whole. Documentation should clearly state which assertions are covered by controls.)	Link to planned controls work	(Yes / No)	Link to planned IT controls work	Link to the related Specific Risk on the Significant Risks Testing Plan				Where assertions are not covered by controls assurance (which is typically the case for classification), additional procedures will need to be set out herein.	Link
Accounts payable			Existence												

Rights and obligations	Completeness	and allocation

Assertions about classes of <u>transactions</u> and events for the period under audit

Occurrence	O	Transactions and events that have been recorded have occurred and pertain to the entity.
Completeness	C	All transactions and events that should have been recorded have been recorded.
Accuracy	A	Amounts and other data relating to recorded transactions and events have been recorded appropriately.
Cut Off	Cu	Transactions and events have been recorded in the correct accounting period.
Classification	Cl	Transactions and events have been recorded in the proper accounts.
Regularity	R	Financial transactions are in accordance with the legislation authorising them, regulations issued by a body with the power to do so under governing legislation, Parliamentary authority and HM Treasury authority.

Assertions about account <u>balances</u> at the period end

Existence	E	Assets, liabilities, and equity interests exist.
Rights and obligations	R&O	The entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
Completeness	C	All assets, liabilities and equity interests that should have been recorded have been recorded.
Valuation and allocation	V	Assets, liabilities and equity interest are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

Assertions about presentation and disclosure

Occurrence	O	Disclosed events, transactions and other matters have occurred
Rights and obligations	R&O	Disclosed events, transactions and other matters pertain to the entity
Completeness	C	All disclosures that should have been included in the financial statements have been included
Classification and Understandability	Cl&U	Financial information is appropriately presented and described, and disclosures are clearly expressed
Accuracy and Valuation	A&V	Financial and other information is disclosed fairly and at appropriate amounts

Annex- H

Materiality, Performance Materiality and expected error

Application of Materiality in the Audit Process

1. There are three main factors which have to be considered when determining whether a matter is material: value, nature, and context. Thus it may not always be the value of an item which primarily determines what is material; but the very nature of the item or the context in which it occurs. Items may be material individually, or in total and certain parts of an account may be of more interest than others to the user(s).

2. Materiality plays an important part at two key stages of the audit process. The aspects of value, nature, and context will influence the role of materiality at these stages in different ways.

Materiality at the Planning Stage

3. The auditor's aim should be to have a reasonable expectation of detecting material errors, omissions, or misstatements in the account, should they exist. Setting an appropriate planning materiality (coupled with the appropriate risk analysis) should satisfy that expectation. At the planning stage, materiality by value is likely to be the main determinant; materiality by nature and context normally are not considered, except in very general terms. To set materiality by value, the auditor should attempt to determine the highest level of error or misstatement that might be tolerated by the perceived users of the accounts. The level set is a matter of judgement. Guidelines in the form of percentage range limits can be used to assist in the judgement process and to achieve a level of consistency.

Sensitivity

4. Sensitivity deals with the consequences of errors on loss of future revenue, the level of public interest in the accounts, etc. Sensitivity is normally not a factor that is taken into account when setting materiality. Rather, it is a factor that is taken into account when assessing audit risk and potentially inherent risk as well. Also taking sensitivity into account when assessing materiality would be erroneously double-count the factor.

5. As discussed further below, there may be exceptional circumstances where a matter is so sensitive that it would affect the user’s perception of what is material. In that case, the

auditor would need to take sensitivity into account when determining the materiality amount.

Setting Planning Materiality

6. The auditor normally selects one overall amount for planning materiality. This recognizes that the audit opinion relates to the financial statement as a whole and the results in each area need to be given the appropriate level of attention relative to its significance to the account as a whole.

7. Auditors also normally select one overall amount for a very practical reason. It is normally not possible to audit one component to a different materiality amount than another component, for several reasons:
    - Components are inter-related. Revenues and cash receipts, for example, come from the same transaction cycles, as do purchases, payables and payments. One cannot use one amount to audit revenues and other cash.
    - There may be misclassifications in the accounts. For example, an expenditure may be recorded as a reduction in revenue, or an operating expenditure may be included in capital expenditures. Given these possibilities, it is not possible to audit expenditures and revenues (or various classes of expenditures) to different materiality amounts.
8. There may be instances where one part of the financial statement that is considered to be so sensitive that it will affect the users' perception of materiality. In such cases, given the fact that components are interrelated and the auditor needs to worry about misclassifications, the auditor would normally need to audit the entire financial statement to the lower materiality amount. In exceptional circumstances, though, the auditor may be able to isolate the relevant balances and transactions and audit just them to a lower materiality amount.

9. In determining materiality by value we attempt to assess the highest level of error across the financial statements as a whole that we would expect the user to tolerate. In doing this we need to take into account the particular characteristics of the entity we are auditing and the interest shown in them by parliament or concerned ones. We do not, therefore, prescribe a fixed level of materiality in either absolute or relative terms which must be applied in all cases. Nevertheless, in line with most audit organizations, we offer range limits to help inform judgement and achieve a level of consistency across all the financial statements we audit.
10. In all cases the audit working paper should clearly demonstrate the reasons for setting materiality at any given level. The ranges need to be applied intelligently and are no substitute for potential judgement based on a thorough understanding of the entity's

activities and the interest shown in them by parliament. In applying them we should always begin by asking ourselves two questions:

- What are the users (such as Parliament) most likely to be concerned about?
- What level of accuracy could the users reasonably expect?

11. Based on the above, when setting materiality, the auditor often uses the following process:
    a) Identify probable users of the financial statements.
    b) Identifying the classes of users with the most exacting standards of precisions which are most significantly affected by the financial statements.
    c) Identify the information in the financial statements that is most important to these users (e.g., cash flow, revenue or expenditure, etc). One or more of these amounts may serve as the base for computing the measures of auditing materiality.
    d) Determine the highest percentage of the base amounts that could be in error without significantly affecting the decisions of the users of financial statements.
    e) Apply that percentage, or lower one, to the base amount to compute the measures of planning materiality.

12. The main users for most national accounts audited by the OCAG will be the national elected body, or central authority, and the extent to which they may be interested in, or influenced by, the information contained in the accounts will often be the major factor affecting the calculation of materiality for the account or its component parts. There may be other significant users, such as the general public, and the auditor should consider whether their interests also affect the materiality decisions for other accounts and the prime users will generally be the governing body.

13. It should be noted that the materiality amount that is determined at this step of the general planning phase is used for the audit of all components, all financial statement assertions and related compliance with authority objectives, etc. There is no need to allocate the amount to the various financial statement components, etc. or to use a lower 'test materiality' amount.

14. The materiality level and the basis for determining it should be documented and approved by the appropriate department head.

15. Our determination in the planning process of the tolerable level of error (i.e. the level of misstatements which would be considered material) provides a basis for:
    a) determining the nature, timing and extent of risk assessment procedures;
    b) identifying and assessing the risks of material misstatement; and
    c) determining the nature, timing and extent of further audit procedures.

Guidelines

16. Determining the materiality level is always relative and always requires judgement; therefore, it is usually not possible to lay down specific rules or absolute numerical measurements that will be valid in every case. Despite this, though, various guidelines have been developed that can be used to assist in the exercise of professional judgement. These guidelines can be used as a way of arriving at the one overall planning materiality amount to be used on the audit.

Determining Materiality and Performance Materiality for the financial statements as a whole

17. The appropriate level of materiality for an audit is a matter of professional judgement. The materiality for the financial statements as a whole may be set using as a starting point a percentage of one or more benchmarks in the financial statements, such as:
    - total costs
    - net costs (expenses less revenues or expenditure less receipts)
    - total assets
    - net assets
    - total equity

18. This is sometimes referred to as **quantitative materiality**, as it is largely based on quantitative factors while taking into account broader considerations through the selection of the appropriate benchmark and percentages to apply.

19. The appropriate benchmark or benchmarks to use will be affected by a number of factors, including (Ref: ISA 320 para A4):
    - the elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses);
    - whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused;
    - the nature of the entity, where the entity is in its life cycle, and the industry and economic environment in which the entity operates; and
    - the relative volatility of the benchmark.

20. Public bodies audited by the OCAG are generally expenditure-driven meaning gross expenditure is often the most appropriate benchmark for setting materiality. Audits of Ministry financial statements should have materiality set on the basis of gross expenditure, rather than on cash funding figures.

21. If one-off items give rise to an exceptional increase or decrease in a benchmark in the current period, it may be appropriate to use a normalised figure for the purposes of assessing materiality. Accordingly, we would normally consider current period, prior period, and budget or forecast financial results and position in assessing materiality.

22. The OCAG considers materiality in the context of a series of ranges of percentages of benchmarks. The ranges we normally apply in the OCAG are 0.5 per cent to 1 per cent of gross expenditure/turnover or gross assets and 5 percent to 10 percent of average surplus or profit with a presumption towards lower levels of materiality in large accounts. This is summarised in the table below:

Range Base	0.5%	1%	2%	5%	10%
Gross expenditure				Increased Sensitivity	
Turnover/income	**Consider**				
Gross Assets	**Consider**				
Average Surplus				**Consider**	

23. Other measures such as net expenditure (after income) or net assets may be appropriate for particular entities.
24. The auditor should select materiality on the basis of a consideration of the different bases available and the particular circumstances of the entity.
25. ISA 450 requires the reassessment of materiality prior to the evaluation of errors. It is usually preferable to set materiality based upon taking account of a range of bases, rather than based upon a fixed percentage of a single base, to reduce the risk of materiality no longer being appropriate if an adjustment is required to the current year figures. Example: setting materiality on a range of bases of budgeted expenditure is Tk. 9,50,00,000 (prior year actual Tk.9,80,00,000). Budgeted gross assets are Tk. 7,00,00,000 (prior year Tk.7,50,00,000). Materiality was assessed at the planning stage as Tk.9, 00,000 considering the benchmarks together (rather than taking 1% of expenditure). At year-end, actual out turn was Tk. 8,90,00,000 and gross assets Tk.7,20,00,000. Planning materiality was assessed as continuing to be appropriate.
26. Usually a single materiality figure is set for all primary statements. However, it may be that where an entity is primarily intended to hold public assets, the interest of the users of the accounts are primarily in relation to the balance sheet (or the income and expenditure statement) in which case it may be appropriate to use a single materiality figure.
27. If two materiality figures are to be used then audit tests should be carefully planned to take account of the impact of balance sheet items on the income and expenditure statement.

Performance Materiality

28. In addition, the auditor should determine the Performance Materiality which will be used for the purposes of assessing the risks of material misstatement and planning the nature, timing and extent of our audit procedures.

29. "Performance Materiality" is equivalent to planning precision, and the terms are used interchangeably herein.
30. We plan the audit based upon Performance Materiality in order to leave a margin for undetected misstatements. The appropriate level to adopt involves professional judgement, and should reflect our understanding of the entity (including any additional information obtained during our risk assessment procedures), prior period misstatements, and our expectations of current period misstatements. (Ref: ISA 320 para A12)
31. Performance Materiality is normally set at 90% of (materiality less expected error). This ensures that sufficient evidence is obtained in support of the audit opinion.
32. The expected level of error in the financial statements is a matter of professional judgement, which is influenced by a number of factors including:
    - the level of errors identified by the prior year audit (including both adjusted and unadjusted errors);
    - whether we expect the client to have corrected unadjusted prior year misstatements;
    - the quality of the entity's control environment; and
    - whether we expect the entity to adjust for identified misstatements in the current year financial statements.
33. In the absence of other indications of the likely level of error in the financial statements, it may be appropriate to use the prior year level of errors identified in the income and expenditure statement as the expected level of errors.
34. In some circumstances, misstatements below the materiality for the financial statements as a whole may be reasonably expected to influence users of the accounts. If this is the case, the auditor should also determine a lower materiality level or levels to be applied to the particular classes of transactions, account balances or disclosures affected. (Ref: ISA 320 pA2-A11)

(a) Example: Calculation of Performance Materiality

- Materiality is TK 5,00,000
- The expected error for the financial statements as a whole is Tk. 1,50,000
- Performance Materiality might therefore be set at (Tk. 5,00,000 – Tk. 1,50,000) X 90% = Tk.3,15,000.

(b) Example: Calculation of Performance Materiality where difficult to revise Materiality

The entity has a number of accounting locations around the country which are material to the financial statements. In practice, any testing needs to be performed at local locations due to the entity's accounting and document management systems. The auditor, therefore, considered that it was appropriate to increase the extent of work to reduce the possibility that testing might need to be extended due to identification of errors from testing. Performance Materiality was, therefore, set at 80% of Materiality less expected error:

- Materiality is Tk. 5,00,000
- The expected error for the financial statements as a whole is Tk. 1,50,000
- Performance Materiality might, therefore, be set at (Tk. 5,00,000–Tk. 1,50,000) X 80% = Tk. 2,80,000.

35. A higher Performance Materiality reduces the planned scope of work, but increases the risk that actual errors will exceed the expected error rate and thus require additional testing to be performed when the results of testing are assessed. Performance Materiality should not be set at a level higher than 90% of Materiality.

36. Setting a lower Performance Materiality increases the planned scope of work. However, this may be appropriate if it would be particularly costly or impractical to extend testing if issues are identified (for example, due to an entity having a tight reporting timeframe, or many locations). When this is the case, the auditor may consider it appropriate to set a lower Performance Materiality. Performance Materiality would not normally be set below 80% of Materiality less Expected Error.

37. It is usually more efficient to be prudent in the level of expected error used in setting Performance Materiality rather than risking having to extend testing if actual errors exceed expected errors.

38. If a lower materiality is set for certain audit areas, a lower Performance Materiality should also be established for those areas. Factors indicating a lower materiality for certain audit areas may be appropriate. Para A10 of ISA 320 states, "Whether law, regulation or the applicable financial reporting framework affect users' expectations regarding the measurement or disclosure of certain items (for example, related party transactions, and the remuneration of management and those charged with governance)".

39. The key disclosures in relation to the industry in which the entity operates (for example, research and development costs for a pharmaceutical company).

40. Whether attention is focused on a particular aspect of the entity's business that is separately disclosed in the financial statements (for example, a newly acquired business)."

41. There may be disclosures in financial statements which are effectively tested on a 100% basis with an expectation that the amount disclosed will be precise. These are typically:

    - senior staff or board members' remuneration;

- particulars of losses that require separate disclosure;
- audit fee;
- prior year figures;
- details of special payments, write-offs and losses;
- specific legal settlements; and
- amounts which should be agreed to other accounts.

Impact of Materiality on Extent of Testing

42. The lower the materiality, the greater the amount of work. Lowering the materiality amount normally results in:
    - Larger sample sizes for both tests of controls and for substantive tests of details;
    - More items become high value transactions needing to be audited 100%;
    - Lower amounts being used for determining which fluctuations found during analytical procedures need to be followed up.
43. Lowering the materiality amount can also increase the chances of the auditor having to issue a reservation of opinion. The maximum error that the auditor can tolerate at the evaluation phase (the Upper Error Limit – UEL) cannot exceed the materiality amount.

Trivial misstatements

44. ISA 450 requires the auditor to accumulate identified misstatements unless they are clearly trivial and so the accumulation of such amounts clearly would not have a material effect on the financial statements. The guidance as to what is clearly trivial is given in para A2 of ISA 450 as :
    "*Clearly trivial" is not another expression for "not material". Matters that are clearly trivial will be of a wholly different (smaller) order of magnitude than materiality determined in accordance with ISA 320*, and will be matters that are *clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of size, nature or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the matter is considered not to be clearly trivial.*
45. We should establish and include in our documentation the level below which misstatements, unless qualitatively more significant, would be regarded as clearly trivial. The level at which misstatements would be regarded as clearly trivial would normally be in the range 1-2% of materiality. The minimum level for clearly trivial would normally be the level of rounding in the account.
46. The level selected is a matter of professional judgement.

47. When we identify misstatements in the audit, if they are greater than the threshold set they should be accumulated and evaluated.

48. If they are less than the threshold, we should still accumulate and evaluate items which are qualitatively of interest. In particular, misstatements indicative of fraud should be accumulated and evaluated regardless of size.

49. If an item is less than the threshold, we do not need to accumulate or evaluate the misstatement or report it to management or those charged with governance.

Materiality at the Reporting Stage

50. At the reporting stage materiality serves as a condition for evaluating the errors or misstatements uncovered and considering the need for qualification to the audit certificate. It also helps with determining the need to insist on separate disclosure for certain items within the accounts as required by statute or regulations.

51. Throughout the audit and its conclusions, the auditor is required to evaluate the results of his/her tests. Normally, all errors will be aggregated, and extrapolated if appropriate, to give the best estimate of most likely errors in the account. To this should be added an allowance for further possible errors to arrive at the maximum possible error (called the upper error limit in ACL) which could exist in the account, to enable the auditor to establish the degree of assurance necessary for the audit opinion.

Factors Affecting Reporting of Materiality

52. If information comes to light during the audit which would have caused us to have established a different materiality level for the financial statements as whole or individual account areas, we should revise our materiality figure accordingly. (Ref: ISA 320 para A13)

Example: Reductions in materiality for changes in circumstances

We set materiality based upon budgets. An increased need for the entity's services was then identified, leading to approved increased spending in the second half of the year. We, therefore, reassessed materiality to reflect the increased level of activity of the entity. We re-set materiality higher. Then, a machinery of government change was announced which significantly reduced the size of the entity and was implemented before the year-end. We, therefore, reduced materiality to reflect the revised scope of the entity.

53. If materiality is revised to a lower level, the auditor should determine whether it is also necessary to revise Performance Materiality, and whether the nature, timing and extent of the audit procedures remain appropriate.

54. When we evaluate the uncorrected misstatements we have identified, it is possible that misstatements individually or in aggregate below materiality will be assessed as material to the financial statements on qualitative grounds or are indicative of the possibility of other misstatements. Accordingly, when evaluating misstatements, we evaluate the size, nature and cause of misstatements.

55. The quantitative considerations are discussed above. As for qualitative aspect, these are sometimes referred to as "materiality by nature and materiality by context".

Materiality by Nature

56. As the term implies, materiality by nature is concerned with the inherent characteristics of a balance or group of balances rather than just their value. A matter may be material by nature because either:
    a) there are specific disclosure requirements that demand a higher degree of accuracy than would normally be expected;
    b) they are sensitive;
    c) they are expenditures required to be authorized in advance by the Ministry of Finance or any responsible body but have failed to be so authorized;
57. Auditors need to remember that materiality needs to be assessed from the users' point of view. Just because an account balance can be audited to a very exacting amount does not mean that the auditor should do so, or that errors larger than what could reasonably have been expected should be considered to be material errors. For example:
    a) Some items are capable of precise determination (e.g., cash at bank and on hand, bank overdrafts and loans). While any departure from the exact figure would call for justification, this does not mean that the departure is material.
    b) Some items are such that precision is both desirable and achievable (e.g., salaries and wages). Again, though, departures from these amounts do not mean that a material error exists.
58. Similarly, the auditor should not confuse potential misstatements with materiality. For example, the entity may be reporting revenues from customs or excise duties that are approximately the same amount as the previous year, but where it is known that the tariffs had been raised. This is an indication of a potential misstatement, as opposed to something that affects the determination of materiality.

59. Similarly, a change in an accounting policy that might affect the financial statements materially is not something to consider when determining the materiality amount itself – the auditor determines materiality, considers the impact of the change in accounting policy, and then determines if the impact is material. If so, the auditor then ensures that there is appropriate disclosure of the change.

60. Auditors must also not confuse materiality and risk. For example, there may be:
    - significant transactions which are subject to high degree of management involvement;
    - transactions or balances not in the ordinary course of business;
    - suspicious or unusual items, etc;
    - significant accounts or items where there is known to be a high probability of material error;
    - a large number of year-end adjustments.

61. These are areas where there may be a high probability of material error, but are not factors to take into account when setting the materiality amount itself.

Compliance Audit interpretation

62. Compliance Auditors should note that irregular transactions are not automatically material by nature, and the risk of transactions being irregular should be considered in the same way as other considerations of materiality by nature of a balance.

63. The financial information needs of legislators and the public as users of public sector accounts should be considered, with typical considerations being:
    - the need for openness and transparency, for example if there are particular disclosure requirements for senior staff remuneration;
    - public expectations and public interest which might deem separate disclosure of special payments, write offs and losses necessary; and
    - the context in which a matter appears, for example if the matter is also subject to compliance with authorities, legislation or regulations. For example situations where a loss is turned into a deficit or where expenditure limits are exceeded.

Materiality by Context

64. An error, omission or misstatement may not be material by value or by nature but may be important because of the circumstances in which it arises and/or the context in which it occurs. The auditor should also be aware that certain misstatements may be material by context because they affect critical points in the accounts and have the effect of changing the meaning of the account. Here are two aspects of materiality by context.

a) Materiality in the General Context

65. To a large degree what matters most is whether an item is material or not in the general context, that is, in its effect on the view portrayed by the accounts as a whole. This view of materiality accords best with overall definition of materiality, that is, a matter would be regarded as material only if it is likely to distort the general picture revealed by the financial statements. Thus it would be an inexcusable waste of audit time to pursue individual errors of Tk. 5 and Tk. 10 in a batch of payment vouchers of large amounts unless the total of such errors runs into hundreds or thousands of Taka or fraud is suspected.

b) Materiality in the Particular Context

66. The particular context relates to the total of which an item forms part or should form part, e.g. the total of sundry debtors comprising a series of individual debtor balances. Even though an item is not material in the general context, it may nevertheless be material in the particular context and vice versa. Much depends on the nature of the item concerned and its significance in its own right.

67. From the audit organizations point of view the question of materiality may be focused essentially on:
    a) matters which are material regardless of the amount involved, and
    b) matters which are material because of the amounts involved.

68. In the former class fall such matters as items which are material by virtue of their nature, by virtue of statutory requirements, or which are material in principle. In regard to the second category, materiality can only be judged in relative terms depending on the circumstances of each individual case.

Technical Consideration

69. The materiality threshold (standard) should be set at the lowest level of misstatements that users might find unacceptable.

70. The materiality threshold should take account of the requirement of the budgetary authorities and the general public.

71. It may be necessary to revise the planned materiality threshold for an audit because, for example, the overall total value of the financial statements is significantly different from that assumed when setting the materiality threshold at planning stage. The auditor must be properly aware of the need for such revision.

72. The determination of materiality threshold is normally a matter of audit organization policy either as to the precise way in which the threshold is determined and approved as a basic element in audit planning or as to the actual threshold amount for a particular audit.

73. The materiality threshold is used to evaluate the importance of the impact of misstatements uncovered by the audit. The auditor should determine the overall most likely error in the financial statements, adding an allowance for further possible error to get a maximum possible error (called the upper error limit), and comparing this total to the materiality threshold.

74. If the estimate of the upper error limit exceeds the materiality threshold the auditor has several choices which are discussed later in the 'evaluation' phase. These include carefully re-examining all his/her evidence, including the possible range of error in statistical estimation procedures and extrapolation, with a view to qualifying his opinion on the financial statements covered by the audit.

75. As the auditor's judgements in relation to materiality threshold, both prior to and throughout the audit are fundamental to the conduct of the audit and to the final interpretation of its results, such judgements should be thoroughly documented in the working paper and subjected to careful management review and approved.

Summary

76. To summarize, setting materiality is, therefore, a decision which requires the auditor to exercise his judgement about the importance of errors to the user of the accounts. There is no prescriptive rule to fit all cases. The audit is planned in totality to provide reasonable assurance that errors or misstatements do not remain in the account above the level which the auditor considers acceptable, but within this overall position there may be misstatements which, because of their particular significance, will need to be considered separately. Apart from statutory and other specific requirements the overriding consideration will usually be their importance to the primary users of the accounts.

Documentation requirements

77. The Engagement Team should document the values used for, and the factors considered in determining:

- materiality for the financial statements as a whole;
- if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures;
- performance materiality; and
- any revision of [the above] as the audit progresses.

78. We should also document the amount below which misstatements would be regarded as clearly trivial, and how we have communicated this to those charged with governance.
79. The Materiality Determination Form at Annex H1 is designed to enable the Engagement Team to document the above.

Expected Total Errors

80. Before leaving the subject of materiality, there is one other matter that the auditor needs to consider at this stage of the audit – total expected errors. To illustrate, assume that the auditor selects a sample and concludes that the most likely error (MLE) in the sample is Tk. 15,00,000. If materiality is Tk. 30,00,000, does the auditor have an acceptable result? The answer is "it depends". Because the auditor has only selected a sample, there is a chance that the actual error in the population is larger than Tk. 30,00,000. What the auditor needs to do is to ensure that he/she has sufficient assurance that the maximum possible error (called the upper error limit) in the population is less than the Tk. 30,00,000 materiality amount.

81. To do this, when planning and performing many analytical procedures and substantive test of details, the auditor reduces the materiality amount by his/her estimate of the most likely error that will exist in the financial statements as a whole. This estimate is referred to as the "expected total errors."

82. To determine the expected total errors, the auditor should consider:

- The errors found in previous years;
- The strength of the control environment and the internal control systems, and changes that the entity has made to them to prevent these errors from recurring or to detect and correct them; and
- Other changes to the entity's business or its internal control structure that could affect the size of the errors.

83. Earlier we noted that the materiality amount that is determined at this step of the general planning phase is used for the audit of all components. There is no need to allocate the amount to the various financial statement components. Consistent with this approach, the expected total errors being used for a particular test must be the expected total errors in the financial statements as a whole, and not just the expected error in the population being audited. When auditing the completeness of income tax receipts, for example, the auditor would need to allow for errors not only in that test, but for errors found in other tests of income tax receipts and for errors found in other financial statement component.

MATERIALITY DETERMINATION FORM

Data should be entered in cells shaded yellow. Hyperlinks to detailed documents should be provided where relevant.

<u>Quantitative considerations</u>

At the planning stage use expected full year position

Materiality base	Current year (Taka)	0.5%	1%	5%	10%
Gross expenditure		-	-		
Turnover/ income		-	-		
Net expenditure (after income) (if relevant)		-	-		
Assets		-	-		
Surplus				-	-
Other (specify if required))		-	-	-	-

Rationale for materiality selected including for the benchmark or benchmarks used

Chosen materiality	-	
Anticipated Most Likely Error for account	-	
Additional safety margin	-	(typically the additional safety margin would set Performance Materiality at 90% of Materiality less Anticipated MLE for the account - amend as appropriate)
Memo - total anticipated error	-	
Chosen level of Performance Materiality	-	

Rationale behind expected level of error and percentage used in setting Performance Materiality

Percentage of materiality considered clearly trivial (normally 1-2% materiality)

Clearly trivial -

Comments on level of misstatement considered clearly trivial

<u>Qualitative considerations</u>

Detail below any considerations of materiality by context or nature:

<u>Account Areas with lower level of materiality and Performance Materiality</u>

The following areas have been determined by the auditor to be appropriate to test to a lower level of materiality and Performance Materiality

Performance materiality is set pro-rata to the reduction in materiality for the balance - amend manually if a different level is appropriate

Account area (and assertion if relevant)	Materiality (Taka)	Performance Materiality (TK.)	Rationale for level selected
None			
		-	
		-	
		-	

Analytical Procedures

Introduction

1. Substantive analytical procedures consist of evaluations of financial information through analysis of plausible relationships between both financial and non-financial data. Substantive analytical procedures also involve any investigation necessary into identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount. (Ref: ISA 520 para A1-A3).

Nature of Analytical Procedures

2. Analytical procedures include a variety of techniques used by the auditor to study relationships between data and to test their plausibility. The data may be on financial as well as non-financial and may arise from internal and external sources. In broad terms, analytical procedures involve looking at figures in the financial statements to see if they are consistent with each other and with the auditor's knowledge of the organization and its activities.
3. The auditor can employ analytical procedures where it can be assumed that there are relationships between items in the financial statements and between items in the account and non-financial data. Analytical procedures include a range of specific techniques:
    - The study of changes in account balances over prior periods leading to a prediction for the current period (e.g., the regular repayment of a loan over XX years);
    - the comparison of financial information with anticipated results (e.g. examining performance variances against budgets and forecasts);
    - the study of relationships between account balances over time;
    - the computations that give a prediction of a given account balance (e.g., using independent data on staff numbers and average pay rates to predict the total staff costs for the period, and using farm data to predict per hectare payments to farmers);
    - the study of relationships between financial and non-financial information, which may confirm the auditor's understanding of the financial information or direct his/her attention towards unusual or unexpected account figures (e.g., license

income against the number of licenses, or agricultural storage costs against records of physical stocks).

4. Various methods may be used in performing the above procedures. These range from simple comparison to complex analysis using advanced statistical techniques. Analytical procedures may be applied on consolidated financial statements, components of financial statements and individual elements of financial information. The auditor's choice of procedures, methods and level of application is a matter of professional judgement.

5. Analytical procedures assist the auditor to:
   - understand the entity's business, including current year transactions and events
   - identify account balances or transaction that may have high inherent or control risks;
   - identify and understand the significant accounting policies; and
   - determine the nature, timing and extent of other audit procedures to be performed.

6. Where we are able to develop a reliable expectation to compare the recorded amounts against, Substantive Analytical Procedures can provide sufficient appropriate audit evidence to provide assurance:
   - on their own for assertions not affected by Specific Risks; or
   - in combination with tests of controls or tests of detail for Specific Risks.

7. Substantive Analytical Procedures involve developing an expectation of the value of an income stream, type of expenditure, year-end balance, or disclosure, based upon an understanding of plausible relationships between financial and non-financial data. (Ref: ISA 520 para A1-A3)
8. Where a suitable expectation has been developed and actual results are within a tolerable amount of the expectation, this provides the planned level of substantive assurance.
9. Where fluctuations or relationships are identified that are inconsistent with other relevant information or that differ from expected values by a significant amount, we investigate the reasons for these and either:
   - obtain the planned level of assurance by identifying appropriate evidence to support the explanations received;
   - identify misstatements in the recorded amounts; or
   - (unusually) identify evidence that the identified relationship is not an appropriate basis for Substantive Analytical Procedures and revise our planned approach.

10. We may develop an expectation based upon:
    - comparable information for prior periods;
    - anticipated results of the entity, such as budgets or forecasts, or expectations of the auditor, such as an estimation of depreciation;
    - similar entity information, such as a comparison of cost levels to similar entities;
    - relationships that would be expected to conform to a predictable pattern based on the entity's experience, such as National Insurance as a proportion of salary costs; or
    - relationships between financial information and relevant non-financial information, such as payroll costs to number of employees, number of individuals eligible for a grant, etc.
11. The planned audit approach to each Audit Area should reflect the Engagement Director and Engagement Manager's consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence over each assertion through a combination of tests of controls and substantive procedures, or substantive procedures alone.
12. Where Substantive Analytical Procedures are an effective and efficient source of substantive assurance, the auditor should plan to use them as the substantive procedures required by ISA 330.
13. Depending upon the entity's circumstances, an appropriately designed Substantive Analytical Procedure may provide assurance over any assertion or Audit Area, either on its own or in combination with Tests of detail.
14. However, we should not rely upon Substantive Analytical Procedures alone to obtain assurance over Specific Risks – some assurance should come from controls or from Tests of detail.
15. Substantive Analytical Procedures may be an efficient way to obtain assurance over completeness of expenditure or income (and so also completeness of liabilities and receivables).
16. Substantive Analytical Procedures are unlikely on their own to provide sufficient appropriate evidence for compliance audits. However, this depends upon the circumstances of the entity and the nature of the balance being considered.

    For example, an analytical procedure may not provide sufficient assurance over regularity of grant expenditure, however:
    - a substantive analytical procedure may provide sufficient appropriate audit evidence that payroll expenditure has been within the pay remit for the organisation;

- for an organisation with limited requirements over regularity from authorities, undertaking similar activities to the prior period, substantive analytical procedures over expenditure, combined with an overall review for new types of expenditure and consideration of their regularity, may provide sufficient appropriate audit evidence.

17. When auditing Specific Risks through substantive procedures alone, the extent of tests of detail and Substantive Analytical Procedures may vary to obtain the planned level of assurance. Teams may either:
    - perform Substantive Analytical Procedures with an Assurance factor (AF) of 2.0, and Tests of detail with an AF of 1.0; or
    - perform Substantive Analytical Procedures with an AF of 0.7, and Tests of detail with an AF of 2.3.

18. Although using both Substantive Analytical Procedures and tests of detail require teams to perform two separate tests, this will often provide high quality audit evidence through providing assurance from both analysis compared to appropriately generated expectations, and tests of underlying transactions.

19. The planned approach should reflect the most effective and efficient approach to obtaining the planned levels of assurance.

Viability of Analytical Procedures

20. The extent to which the auditor can use analytical procedures will depend on a number of factors including:
    - The nature of the organization and its operations. Some organizations are very stable and hence comparisons to the previous year, etc. are relatively easy to perform. As such, the current year's account balances and transactions can be predicted with reasonable accuracy.
    - The knowledge of the organization gained from previous audits. Analytical procedures require knowledge of then entity – often more than is required to perform sampling procedures.
    - The availability of appropriate financial and non-financial information from internal and external sources. If the necessary information is not available, then the procedures cannot be performed.
    - The relevance, level of detail and reliability of the various forms of information available. If the available information is not reliable, then the procedures cannot be performed.

- the extent to which the account or the items to be examined can be predicted with reasonable accuracy;
- the comparability and independence of information from different sources. If the data in the accounts being compared are coming from the same source, then the comparison will have limited value.
- Audit team attributes. In order to properly plan, perform and evaluate the results of an analytical procedure, one must have a sound understanding of the entity, the industry and the data being analysed. Should the audit team not possess a sufficient understanding to perform a particular analytical procedure, then the procedure should not be performed.
- The inherent risk and the control risk. The higher these risks, the greater the possibility that the data to be used in the analytical procedure is unreliable. In particular, should management officials be able to override specific internal controls and manipulate the data, they may be able to alter the data so as to hide significant fluctuations, over-expended appropriations, etc.
- The component and the specific financial audit assertion for which audit evidence is required. Analytical procedures are generally more useful in providing assurance for revenue and expenditure accounts than for balance sheet accounts. For example, analytical procedures may be very useful in providing assurance as to the completeness and measurement of many revenue and expenditure accounts. However, they are usually not very good at testing the validity or ownership of assets.
- Related compliance with authority objective for which audit evidence is required. Analytical procedures are often not particularly good at obtaining assurance with respect to most compliance with authority objectives. For example analytical procedures will not be very good at determining if:
    - The services were actually performed or the goods were actually received;
    - The expenditures are consistent with the nature of the appropriation to which they were charged;
    - The expenditures, borrowings or cash received are in accordance with the applicable legislation; or
    - The cash received was for an approved tax or other approved revenue source.

For all of these, a detailed examination of specific expenditure transactions, borrowing transactions, or revenue transactions is normally the best way to obtain assurance with respect to these compliance with authority objectives.

- Analytical procedures are often not particularly good at determining if there are appropriations that have been exceeded but have not been so disclosed. This is because entity officials may simply adjust the books or defer the recording of expenditures to hide such situations. A detailed examination of journal vouchers and the coding on specific transactions, and a detailed review of the year-end cut-off, are normally the best way to obtain assurance with respect to this particular compliance with authority objective
- Costs and benefits of obtaining assurance from analytical procedures. Generally, analytical procedures take less time to apply than a test of details and, therefore, have the potential to be a more efficient source of audit evidence. Cost and benefit considerations include:
    - The ease and cost of obtaining and assessing the reliability of the data to be used in the analytical procedure;
    - The ease and cost of applying the analytical procedure, including obtaining appropriate explanations for all significant fluctuations; and
    - The ease and cost of obtaining assurance from other sources of audit assurance.

Trend Analysis and Ratio Analysis

21. Analytical procedures often are categorized as either trend analysis or ratio analysis.

Trend Analysis

22. Trend analysis looks at changes in a given account balance or financial statement line over past accounting periods.

23. As discussed in more detail below, trend analysis can be performed with various degrees of sophistication/complexity. For example, a simple diagnostic approach may be used where the auditor compares the actual current year value with the past trend to determine if it appears to be out of line. Conversely, a predictive approach may be used where the auditor adjusts the previous years' trend amounts for known changes in order to predict the current year's amount.

24. The more complex techniques are capable of giving more accurate predictions and therefore will provide more substantive assurance than the less complex procedures. However, as techniques increase in complexity; more audit effort is usually required to perform them. A balance has to be struck between the costs and benefits of each technique.

25. Trend analysis techniques include:
    - graphical methods;
    - period to period comparisons;
    - weighted averages;
    - moving averages;
    - statistical time series analysis.

26. Graphical methods and period-to-period comparisons are often appropriate at the planning and review stages of the audit to identify the area of focus.

Ratio Analysis

27. Ratio analysis is a method that involves comparing relevant relationships between financial statement figures. This isolates stable, common or irregular relationships between account balances over a period of time. Ratio analysis is particularly useful where the ratios can be calculated for a sufficient number of years to allow trends to be properly recognized and evaluated.

28. The most commonly used ratio analysis method is financial ratio analysis.

Financial Ratio Analysis

29. Financial ratio analysis involves balances within financial statements to understand the relationship between those balances and help identify changes in the relationship over time. Investigating the relationships between account balances can help auditors to understand the information contained in financial statements.

30. A wide range of financial ratios should be employed by the auditor depending on the nature of the organization and its financial statements. Gross profit margin (operating profit against sales), stock turnover (cost of sales against stock values, and debtor days (trade debtors against total credit sales) are three important ratios commonly examined in a trading organization. Certain financial ratios which involve the measurement of an entity's current assets against its current liabilities can provide a useful measure of its ability to meet its short-term obligations and may direct attention to liquidity problems.

31. Ratio analysis can be an effective technique provided the following conditions apply:
    - the ratios to be compared must be calculated using the same methodology;
    - the account figures in the ratio to be compared are calculated using the same accounting policies;
    - the ratio is expected to be relatively stable between periods.

Categories of Analytical Procedures

32. Analytical procedures can be grouped into five general categories. Each category can involve the use of either trend analysis or ratio analysis.
33. As a general rule, each category can provide a greater amount of assurance than the previous category. However, there are numerous factors, other than the type of analytical procedure being performed, that affects the amount of assurance that can be obtained from a particular procedure. These other factors are discussed below.

Category 1: General reviews for reasonableness

34. This category of analytical procedures involves a high level comparison of current information with that of previous periods, with budgets or with statistics available from the entity. No pre-determined threshold amount is specified for identifying significant fluctuations. The process is sometimes referred to as “eyeballing” the financial statements – the auditor looks for accounts that appear to be unusual in amount, in volume of activity, etc.
35. The objective of this type of analysis is generally attention directing as opposed to obtaining audit assurance.
36. Although this type of analytical procedure normally does not provide any assurance, it can contribute immensely to an understanding of how the entity operates, how different components should interrelate, and how the financial statements should present the underlying events.
37. As a result, general reviews for reasonableness should be conducted during the general planning phase and the evaluation phase of the audit.

Category 2: Comparative analysis

38. This category of analytical procedures involves comparing the current year's reported amounts (or ratios) with those of the prior year (or years). The data from the previous year(s) are not adjusted for known changes in the factors affecting the data. Comparative analysis assumes that the prior year's data provide a sufficiently accurate estimate of the current year's amount and, therefore, can be used to identify any significant fluctuations from the current year's recorded amount. A pre-determined threshold amount is specified for identifying significant fluctuations.
39. For example, the auditor may decide to compare the employee related expenses (pay, allowances, etc.), operating expenses (fees, communications, utilities, etc.) and income tax receipts to the equivalent amounts for the previous year. The auditor would then follow up differences greater than the threshold amount.

40. This type of analytical procedure can provide a low level of substantive assurance.

Category 3: Predictive analysis

41. Predictive analysis involves comparing the current year's reported amounts (or ratios) with a prediction of what the current year's amounts (or ratios) should be based upon the trend of the amounts (or ratios) from the previous year (or years). The data from the previous year(s) are adjusted for all known changes in the factors affecting the data. A pre-determined threshold amount is specified for identifying significant fluctuations.
42. For example, before making a comparison of the employee related expenses for the current year to the equivalent expenses for the previous year, the auditor could adjust the previous year’s amounts for known changes in the average pay scales and in the number of staff within the specific entity for which the comparison is being made.
43. Similarly, before making a comparison of income tax receipts for the current year to the equivalent amounts for the previous year, the auditor could adjust the previous year’s amounts for known changes in income tax rates.
44. Because the prior year’s amounts are adjusted for known changes before the comparison is made, this type of analytical procedure can produce a more precise estimate than would be the case with comparative analysis. As a result, it can provide a higher level of substantive assurance than comparative analysis.

Category 4: Statistical analysis

45. This category of analytical procedures involves analyzing the known behaviour of variables and developing an equation (model) that explains the relationship between these variables. A pre-determined threshold amount is specified for identifying significant fluctuations.
46. For example, the auditor may have reliable monthly payroll expenditure, together with corresponding monthly figures for average numbers of staff in post, for the past few years. It would then be possible to develop a statistical model for the prediction of payroll expenditures in terms of staff numbers and time, and to use this model to predict expenditure in the current period from the corresponding staff numbers. The auditor would input data on employee related expenses for the previous several years into the software package. The software package would then estimate the amount of employee related expenses for the current year.
47. Although this category is similar to predictive analysis, statistical analysis provides more accurate predictions and objectively measures the confidence level and the achieved level of precision of the prediction. As a result, it can provide an even higher level of substantive assurance than predictive analysis.

Category 5: Overall verification procedures

48. This category of analytical procedures involves building up an estimate of an account balance from known and verified (as opposed to analysed) data. For example, the auditor could verify the number of rental units by type of unit, the average rent by type of unit, and the vacancy rate by type of unit. For each type of unit the auditor could then multiply the number of units times the average rent times the vacancy rate and compare the result to the revenue received from the rents.
49. As another example, the auditor could verify the monthly salary for each employee on the payroll and use that data to estimate the total payroll expenditure for salaried employees.
50. A pre-determined threshold amount is specified for identifying significant fluctuations.
51. Overall verification procedures usually result in a very accurate estimate of the account. For this reason, and because the inputs are verified (as opposed to analysed), this category of analytical procedures generally produces a very high level of substantive assurance.

Factors Affecting the Assurance that can be derived from Analytical Procedures

52. The degree of assurance derivable from a particular type of analytical procedure depends on many factors that must be considered by the auditor. Outlined below are the key factors affecting the effectiveness of an analytical procedure.

Category to which the procedure belongs

53. The quality of an analytical procedure depends on the category to which it belongs. As we move from general reviews for reasonableness through to overall verification procedures, a more comprehensive analysis of the underlying relationships is usually performed. This, in turn, results in a greater amount of substantive assurance.
54. While guidelines should not replace the use of professional judgement, the following may be useful for determining the amount of assurance that is usually achievable from each category of analytical procedures:

Type of Analytical Procedure	**Assurance**
General reviews for reasonableness	Nil
Comparative analysis	A = 0.7
Predictive analysis	Up to A = 2.3
Statistical analysis	Up to A = 2.3
Overall verification procedures	Up to A = 2.3

Threshold amount used to determine significant fluctuations

55. If the auditor sets a low threshold amount he/she will have more fluctuations to follow up than if the auditor selected a high threshold amount. As a result, the lower the threshold amounts, the higher the assurance that can be achieved.
56. In setting the amount to be used for identifying significant fluctuations, the auditor should consider the planned precision determined for the audit. The threshold amount to be used for identifying significant fluctuations should be directly related to this planned precision amount.
57. With a statistical analysis software package, the planned precision and the desired level of assurance are keyed in and the software package automatically calculates the amount to be used. For other types of analytical procedures, the auditor must set the threshold amount subjectively using his/her professional judgement.
58. Items comprising an account balance can be analysed using a number of different data profiles. For example, when analysing payroll expenditures for the government, the auditor could analyse the expenditures:
    - For the government as a whole;
    - By ministry, department, and/or agency, etc;
    - By division or by staff classification; and/or
    - For the year as a whole or for each month.

59. Data used can be entity-wide data (e.g., payroll related expenses for the ministry as a whole), disaggregated by one level (e.g., payroll expenditures for each division or by staff category), or disaggregated by two levels (e.g., payroll expenditures for each staff category within each division).

Quality of the relationship

60. The quality of an analytical procedure is only as good as the quality of the underlying relationship upon which it is built. In seeking to identify the quality of a relationship, the factors described in the following paragraphs should be considered.
61. Simplicity of the relationship: The fewer the factors that could cause changes in an account over time, the easier it should be to estimate the current year's balance and follow up significant fluctuations. As more factors are added, it becomes increasingly difficult to design an analytical procedure that will adequately capture each factor's impact on the account.

62. Plausibility of the relationship: A plausible relationship is one that the auditor may reasonably expect to exist based on an understanding of the business and the accounting

Grade	Staff Number	Pay Rate	Predicated Total	Actual Total	Difference	
	No.	Tk.	Tk.		Tk.	%
Secretary	1.0	69,818	69,818	70,234	416	0.60
Additional Secretary	4.0	59,127	236,508	245,510	9,002	3.81
Directors	3.0	48,461	145,383	154,079	8,696	5.98
Assistant Secretary	26.0	44,631	1,160,406	1,198,541	38,135	3.29
Principal	118.5	31,602	3,744,837	3,755,146	10,309	0.28
Staff Officer	376.5	18,450	6,946,452	6,905,384	-41,041	-0.59
Executive Officer	571.5	15,839	9,051,988	9,020,459	-31,529	-0.35
Admin Officer	847.0	10,396	8,805,412	8,952,468	147,056	1.67
Support Grade Band 1	35.0	10,021	350,735	365,946	15,211	4.34
Support Grade Band 2	259.0	8,870	2,297,330	2,304,846	7,516	0.33
Administrative Assistant	1624.0	7,755	12,594,120	12,661,752	67,632	0.54
Etc.		Etc.	Etc.	Etc.	Etc.	Etc.
Total for all grades	7777.5		969,867,127	97,605,433	738,306	0.76

Comparisons against the actual amount and the predicted amount can be seen in the table above. Differences were calculated for each grade as well as the overall difference for all grades combined. Payroll expenditure was predicted at Tk.9,68,67,127 in comparison to an outturn of Tk.9,76,05,433. The outturn was Tk.7,38,306 (0.76%) more than the prediction. This difference was within the tolerable difference of Tk.17,02,610 (1.74%). No material fluctuations were found.

However, there were some significant fluctuations for particular grades. Significant fluctuations for each grade were defined as differences greater than +/-1.75% (the tolerable difference). The highlighted fluctuations were investigated to ensure they were not material by context or nature. Possible discrepancies could also be due to the use of contract staff at a higher or lower level, or a small minority of staff not covered by the main grading structure.

Step 6: Evaluation

The expected value was well within the tolerable range and hence substantive assurance was achieved from the analytical procedure. Fluctuations within grades greater than +/- 2.5% were invested and no material error was found.

Example 2

Step 1: Determine whether it is appropriate to use Substantive Analytical Procedures

Testing the accuracy and completeness of income generated during the year from

b) Independence of the data

71. For data to be independent, each item being used in the analysis should come from a source that is different than the source of the amount being analysed. This ensures a stronger test, as it is unlikely that errors will occur in both sets of data simultaneously.
72. If the items are not coming from an independent source, the auditor would need to verify the completeness and accuracy of the items being used in the analysis.
73. The most independent internal sources are records maintained by different people. Examples would include shipping records, production records, personnel records and similar records that are not part of the basic accounting records.
74. If external data are available and used in the analysis, it would ordinarily satisfy the independence criteria. However, care must still be exercised in determining whether the data is relevant. For example, industry statistics are often several years out of date.

c) Level of data aggregation

75. In general, the less aggregated the data, the better the analysis that will result, and the greater the amount of assurance that can be obtained. This is because the less aggregated the data, the less chance there is that errors in one specific account will be hidden by appropriate fluctuations in other accounts.

    For example, the auditor may decide to simply compare revenues by major category (direct taxes and indirect taxes) to the equivalent amounts for the previous year. A better test would be to do the comparison at a less aggregated level – personal income taxes, corporate income taxes, property taxes, etc.

    As another example, the auditor may attempt to do an overall verification procedure on the total payroll expenditure. The auditor may get data about staff numbers and grades from personnel systems which are maintained independently of data on pay. As a first approximation, the auditor may try to predict total payroll costs in the period by multiplying numbers in each grade by the mid-point of the pay scale for the grade. However, such a method fails to take account of the numbers of staff in each grade at different points on the pay scale. The auditor may be able to use data on lengths of time in the grade to refine the procedures by using a weighted average pay rate for each grade, rather than simply the mid-point of each scale. Even further refinements might take account of other variables, such as annual performance bonuses.

d) Measurement frequency and number of periods of data used

76. Generally, the greater the number of data observations used in the analysis, the stronger the evidence provided through the analytical procedure. The more frequently one can

observe a particular relationship, the more one can be assured of the consistency of the relationship. For example:

- Monthly observations generally provide more useful information (and assurance) than annual observations; and
- Using several years' data in the analysis generally provides more assurance than only using the most recent year's data.

Documentation

77. As with all audit work the auditor should ensure that his working papers adequately document the planning performance and results of and conclusions from analytical review work.
78. Working papers should consist of:
    a) an outline programme of the review work; e.g. account areas to be considered; overall review work on account figures, allocations of time;
    b) a summary of significant figures and relationships;
    c) details of all significant variations considered;
    d) details of the results of investigations into such variations including explanations obtained from management and the steps taken to verify them;
    e) the audit conclusion reached; and
    f) Information considered necessary for assisting with the planning of subsequent audit.
79. The sources and dates of the acquisition of figures used should be clearly indicated. A record of the dates and ratios used for analytical review purposes for each accounts should be kept on audit files.

Planning and Performing Substantive Analytical Procedures

80. Planning and performing Substantive Analytical Procedures requires the Engagement Team to use professional judgement in:
    - determining whether it is appropriate to use Substantive Analytical Procedures;
    - determining whether the data used to develop an expectation is reliable;
    - developing the expectation based upon an identified relationship in the data;
    - determining the tolerable difference;
    - investigating results of Substantive Analytical Procedures; and
    - concluding upon the Substantive Analytical Procedure.
81. Achieving the planned level of assurance is dependent upon the quality of the design of the Substantive Analytical Procedure.

82. The steps involved are discussed further below.

Determine whether it is appropriate to use Substantive Analytical Procedures

83. In planning whether to use Substantive Analytical Procedures to test an Audit Area, the auditor should determine the suitability of particular Substantive Analytical Procedures for each assertion, taking account of the assessed risks of material misstatement and tests of detail, if any, for these assertions. (Ref: ISA 520 para A6-A11)
84. Engagement Teams should only plan to rely on Substantive Analytical Procedures if they give a comparable quality of audit evidence to a test of detail.
85. In general, Substantive Analytical Procedures based upon a predictive model provide higher quality audit evidence than comparative analytical procedures. For example, a Substantive Analytical Procedure using an expectation based upon approved salary bandings for various grades in the organisation multiplied by an audited head-count for each grade provides higher quality audit evidence than one using an expectation based upon total salary expense for the prior year.
86. However, depending upon the circumstances, relatively simple predictive models (such as the above expectation of payroll) or comparative analyses (e.g. vs. prior year adjusted for inflation when level of activity and cost of work performed are validly both expected to remain the same) may be appropriate.
87. The appropriateness of Substantive Analytical Procedures will depend upon the nature of the assertion and our assessment of the risk of material misstatement. For example, if controls over processing of payments are deficient, we may decide to use tests of detail for expenditure rather than substantive analytical procedures.
88. Substantive Analytical Procedures may also be appropriate to perform in combination with tests of detail. For example, when obtaining audit evidence regarding the valuation of accounts receivable balances, we may apply analytical procedures to an ageing of customers' accounts in addition to performing tests of detail on subsequent cash receipts to determine the collectability of the receivables.

Determining whether the data used to develop the expectation is reliable

89. The auditor should evaluate the reliability of data used to develop our expectation, taking account of source, comparability, and nature and relevance of information available, and controls over preparation. (Ref: ISA 520 para A12-A14)
90. The auditor should confirm with management that they consider the relationship used to be a plausible basis for developing an expectation.

91. Factors to consider include:
    - source of the information available - for example, information may be more reliable when it is obtained from independent sources outside the entity;
    - comparability of the information available - for example, broad economic data such as the overall inflation rate may not be appropriate for a department with particular cost pressures;
    - nature and relevance of the information available - for example, whether budgets have been established as results to be expected rather than as goals to be achieved;
    - controls over the preparation of the information that are designed to ensure its completeness, accuracy and validity - for example, controls over the preparation, review and maintenance of budgets; and
    - prior year knowledge and understanding – e.g. knowledge that there have been issues in prior years with the accuracy of a data source.

92. We may consider it appropriate to test the operating effectiveness of controls over the entity's preparation of information used by the auditor in performing substantive analytical procedures – if they are operating effectively, this would give greater confidence in the Substantive Analytical Procedures. The operating effectiveness of controls over non-financial information may often be tested in conjunction with other tests of controls (e.g. controls over payroll may also give assurance over data on headcounts).

Developing the expectation

93. The Engagement Team should develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated. (Ref: ISA 520 para A15)

94. The precision of a Substantive Analytical Procedure is affected by considerations such as:
    - the accuracy with which the expected results of substantive analytical procedures can be predicted - for example, we may expect greater accuracy when predicting payroll costs than when comparing discretionary expenses, such as advertising, to prior periods;
    - the degree to which information can be disaggregated - for example, substantive analytical procedures may be more effective when considering an expectation of salary costs by grade, or by different divisions, rather than the overall salary cost; and

- the availability of the information, both financial and non-financial - for example, we may consider whether financial information, such as budgets or forecasts, and non-financial information is available to design substantive analytical procedures. If the information is available, we should consider its reliability as discussed above.

95. It is unrealistic to expect analytical procedures to predict financial amounts or ratios exactly. Hence expected values, or the range within which they are likely to lie, need to be estimated. To help ensure that any bias that might be introduced by the auditor is limited, the expected values (and/or their range) should be estimated before the analytical procedure is performed.

96. The expected value or its range should be determined using professional judgement. In some cases, where a statistically-based analytical procedure is used, (for example regression analysis), the range can be set to the confidence limits for that expected value. If the estimated range or the uncertainty associated with the expected value is very wide, the Substantive Analytical Procedure may not be able to provide adequate assurance that the actual amount is not materially misstated.

97. A more complex procedure, with accurate and detailed input data, and a more complex model will usually provide higher precision and hence a higher level of assurance.

Determining the tolerable difference

98. The auditor should determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation. This is termed as the 'tolerable difference'. (Ref: ISA 520 para A16)

99. The tolerable difference should be determined before comparing the expectation to the recorded amount.

100. The level of assurance that is to be obtained from any Substantive Analytical Procedure is dependent upon the amount of assurance needed from that procedure to reduce audit risk to a specified level. The risk assessment performed at the planning stage, as well as results of other audit procedures, should be used to determine the level of assurance required from the analytical procedure. As the level of assurance increases, the corresponding level of precision required for the analytical procedure should also increase.

101. It is not possible to use Substantive Analytical Procedures on their own to obtain assurance over Specific Risks (i.e. Substantive Analytical Procedures cannot be performed with an AF of 3.0).

Substantive Analytical Procedures with AF of 2.0

102. If performing Substantive Analytical Procedures to obtain an Assurance Factor of 2.0, the tolerable difference is given by:

where

Materiality = the materiality level of the whole account

Actual Amount = the recorded amount that is being audited (i.e. the figure recorded in the accounts)

Materiality Base = the value used to calculate materiality, e.g. Gross Expenditure

The tolerable difference is capped at 90% of Performance Materiality. For example, in cases where the account area value can exceed the materiality base (for example, where the surplus generated by an entity is adopted as the most appropriate materiality base) the tolerable difference should be set at 90% Performance Materiality.

Substantive Analytical Procedures with AF of 0.7

103. If performing Substantive Analytical Procedures to obtain an Assurance Factor of 0.7, the tolerable difference is given by setting a percentage of 10-25% of the recorded amount, capped at Performance Materiality. The auditor should use professional judgement in the context of the circumstances in the audit to determine what an appropriate threshold percentage is.

Substantive Analytical Procedures for non-significant balances

104. If performing Substantive Analytical Procedures over non-significant balances, the auditor should set tolerable error at the lower of Performance Materiality or 25% of the recorded amount. The Substantive Analytical Procedure may be based upon a simple comparison to prior year if the auditor considers this to be effective and efficient. Example: auditing a non-significant other payables balance. Other payables is a non-significant balance of TK. 10,00,000 (prior year TK. 12,00,000) made up of deposits on a number of leases which mostly have several years to run. One lease expired in the year and the client exited the premises. The auditor has tested with a comparative substantive analytical procedure comparing to prior year less the lease expiring in the year, with a tolerable difference of Tk. 2,50,000 (25% of recorded amount).

Investigating Results of Substantive Analytical Procedures

105. The auditor should compare the recorded amount to the expectation that they have developed.

If:

- the variance between recorded amount and expectation is within the tolerable difference; and
- there are no fluctuations or relationships apparent from the analysis which are inconsistent with other audit evidence or expectations;

then the Substantive Analytical Procedure has provided the planned assurance.

If:

- the variance between recorded amount and expectation is greater than the tolerable difference; or
- the auditor identifies fluctuations or relationships apparent from the analysis which are inconsistent with other audit evidence or expectations,

then the auditor should investigate the differences.

106. The auditor should:

a) Inquire of management as to the reasons for the differences, and obtain appropriate audit evidence relevant to management's responses; and

b) Perform other audit procedures as necessary in the circumstances. (Ref: ISA 520 para A20-A21)

107. The auditor may be able to evaluate management's responses in the context of his/her understanding of the entity and other audit evidence obtained, or he/she may need to obtain additional audit evidence to support their explanations.

108. If management's explanations indicate that there are additional factors that should have been considered in establishing his expectation, he will usually revise the expectation and evaluate whether the revised expectation and recorded amount are within tolerable difference.

109. The evidence supporting revised expectation should be of equivalent quality to initial expectation.

110. On occasion auditor may go through more than one cycle of this process before arriving at an audit conclusion.

Concluding on Substantive Analytical Procedures

111. If management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate, the auditor should consider whether a misstatement has been identified.

112. If auditor do not consider there to have been a misstatement identified, he may conclude that the identified relationship is not an appropriate basis for Substantive Analytical Procedures and revise his planned approach to include alternative substantive procedures.

113. Auditor should not automatically adopt an alternative approach without understanding why the relationship identified was inappropriate.

Consideration of misstatements

114. If auditor identified a misstatement, he should consider whether he has achieved the planned level of assurance or whether additional procedures are required. If the misstatement identified exceeds the expected error rate assessed at the planning phase (i.e. is greater than Materiality – Performance Materiality), he should clearly document his rationale for conclusion on the adequacy of the scope of work performed.

115. As substantive analytical procedures are effectively 100% tests of an assertion, auditors will usually provide the planned level of assurance even if they detect a misstatement which exceeds the expected error rate for the audit identified at planning stage (i.e. a misstatement greater than the difference between Materiality and Performance Materiality).

116. Auditors should understand the nature and cause of the misstatement and determine whether they indicate that other misstatements may exist.

117. This may be due to a previously unidentified Significant Risk.

118. Indications that other misstatements may exist include if a misstatement arose from a breakdown in internal control, or from inappropriate assumptions or valuation methods that have been widely applied by the entity.

119. If there is a risk that other misstatements may exist that, aggregated with identified misstatements, may be material, then the auditor should revise the Overall Audit Strategy and the Audit Plan.

Example 1

Step 1: Determine whether it is appropriate to use Substantive Analytical Procedures

Confirming the accuracy and completeness of payroll expenditure, during the interim stage of the audit to obtain substantive assurance. Reasonableness testing using modelling techniques to predict payroll would achieve the required level of assurance.

Step 2: Determine whether the data used to develop the expectation is reliable

Independent personnel records relating to payroll were available from Human Resources within a computerised format, allowing the data to be obtained and manipulated efficiently. It would be reasonable to use this data to predict a relationship with payroll, and auditor usually checked a small sample of 5 items for accuracy.

Step 3 Develop the expectation

Independent data obtained included; 1) staff numbers by grade, 2) pay scale for each grade, 3) length of time in each grade. The same rates of pay were applied throughout the year. A weighted average pay rate was calculated for each member of staff, using the length of time spent in that grade. This produced an estimate of the average position on the relevant pay scale according to grade for each member of staff. The addition of the individual averages by grade produced the estimated aggregated payroll profile.

Step 4: Determine the tolerable difference

The planned level of precision specified using the tolerable difference formula is given below .

$$\text{Tolerable difference} = \text{Materiality} \times \sqrt{\frac{\text{Actual Amount}}{\text{Materiality Base}}}$$

Figures from the account displayed the following; Actual Amount = Tk. 9,76,05,453, Materiality Base = Tk. 29,70,00,000 and Materiality = Tk. 29,70,000. Therefore:

$$\textbf{Tolerable Difference} = \text{Tk. } 29{,}70{,}000 \times \sqrt{\frac{\text{Tk. } 9{,}76{,}05{,}453}{\text{Tk. } 29{,}70{,}00{,}000}}$$

$$= \text{Tk. } 77{,}02{,}610 \text{ or } 1.74\%$$

Step 5: Investigate results of analytical procedures (including significant fluctuations)

An extract of the results for a selection of grades, together with summary data for all grades are given in the table below.

Grade	Staff Number	Pay Rate	Predicated Total	Actual Total	Difference	
	No.	Tk.	Tk.		Tk.	%
Secretary	1.0	69,818	69,818	70,234	416	0.60
Additional Secretary	4.0	59,127	236,508	245,510	9,002	3.81
Directors	3.0	48,461	145,383	154,079	8,696	5.98
Assistant Secretary	26.0	44,631	1,160,406	1,198,541	38,135	3.29
Principal	118.5	31,602	3,744,837	3,755,146	10,309	0.28
Staff Officer	376.5	18,450	6,946,452	6,905,384	-41,041	-0.59
Executive Officer	571.5	15,839	9,051,988	9,020,459	-31,529	-0.35
Admin Officer	847.0	10,396	8,805,412	8,952,468	147,056	1.67
Support Grade Band 1	35.0	10,021	350,735	365,946	15,211	4.34
Support Grade Band 2	259.0	8,870	2,297,330	2,304,846	7,516	0.33
Administrative Assistant	1624.0	7,755	12,594,120	12,661,752	67,632	0.54
Etc.		Etc.	Etc.	Etc.	Etc.	Etc.
Total for all grades	7777.5		969,867,127	97,605,433	738,306	0.76

Comparisons against the actual amount and the predicted amount can be seen in the table above. Differences were calculated for each grade as well as the overall difference for all grades combined. Payroll expenditure was predicted at Tk.9,68,67,127 in comparison to an outturn of Tk.9,76,05,433. The outturn was Tk.7,38,306 (0.76%) more than the prediction. This difference was within the tolerable difference of Tk.17,02,610 (1.74%). No material fluctuations were found.

However, there were some significant fluctuations for particular grades. Significant fluctuations for each grade were defined as differences greater than +/-1.75% (the tolerable difference). The highlighted fluctuations were investigated to ensure they were not material by context or nature. Possible discrepancies could also be due to the use of contract staff at a higher or lower level, or a small minority of staff not covered by the main grading structure.

Step 6: Evaluation

The expected value was well within the tolerable range and hence substantive assurance was achieved from the analytical procedure. Fluctuations within grades greater than +/- 2.5% were invested and no material error was found.

Example 2

Step 1: Determine whether it is appropriate to use Substantive Analytical Procedures

Testing the accuracy and completeness of income generated during the year from tickets issued for an exhibition held within a museum. Modelling techniques accounting for variations in ticket type and price would produce an estimate for income to achieve the required level of assurance.

Step 2: Determine whether the data used to develop the expectation is reliable

Independent data on the number of tickets issued by type were available from a computer system that sequentially numbered each ticket. Simple manipulation of the system would determine the exact number of issued tickets and hence it would be reasonable to use this data source.

Step 3: Develop the expectation

Independent data obtained included (1) number of tickets issued by type for each month, (2) the price of each ticket by type. The same charges of each ticket were applied throughout the year. The numbers of tickets sold were multiplied by the price of the ticket to give an income amount for each month. The addition of the individual monthly estimates produced the aggregated income total.

Step 4: Determine tolerable difference

Figures from the account displayed the following: Actual Amount = Tk. 53,239 Materiality Base = Tk.8,66,489 and Materiality = Tk.8,665. Hence

Tolerable Difference

$$= \text{Tk. } 8{,}665 \times \sqrt{\frac{\text{Tk. } 53{,}239}{\text{Tk. } 866{,}489}}$$

$$= \text{Tk. } 2{,}148 \text{ or } 4.03\%$$

Step 5: Investigate results (including significant fluctuations)

The results from the prediction for each month and ticket type are given in the table below.

Month	Ticket Sales by Type		Price (TK.)		Predicated Income (TK.)
	1 Day	4 Day	1 Day	4 day	
January	32	16	22	35	1,264
February	44	52	22	35	2,788
March	48	52	22	35	2,876
April	44	92	22	35	4,188
May	108	60	22	35	4,476
June	52	100	22	35	4,644
July	116	216	22	35	10,112
August	96	80	22	35	4,912
September	76	60	22	35	3,772
October	68	36	22	35	2,756
November	44	40	22	35	2,368
December	60	56	22	35	3,280
Total	788	860			47,436

Comparisons against the outturn annual income of Tk. 53,239 and the predicted income of Tk. 47,436 showed there was a difference of Tk. 5,803 or 10.90%. This significant difference was larger than the tolerable difference of Tk. 2,148 or 4.03%. Hence a material fluctuation was found and needed to be investigated.

Further examination of the records showed that the prices for both a 1 day and a 4 day pass were increased from July that year and the initial estimate did not reflect this. The results from the adjusted predictions are given in the table below.

Month	Ticket Sales by Type		Price (TK.)		Predicated Income (TK.)
	1 Day	4 Day	1 Day	4 day	
January	32	16	22	35	1,264
February	44	52	22	35	2,788
March	48	52	22	35	2,876
April	44	92	22	35	4,188
May	108	60	22	35	4,476
June	52	100	22	35	4,644
July	116	216	25	40	11,540
August	96	80	25	40	5,600
September	76	60	25	40	4,300
October	68	36	25	40	3,140
November	44	40	25	40	2,700
December	60	56	25	40	3,740
Total	788	860			51,256

A comparison of the outturn income against the adjusted prediction showed a difference of Tk.1,983 or 3.72%. This difference is now within the required tolerable difference.

Step 6: Evaluation

The adjusted predicted value was within the tolerable range and hence substantive assurance was achieved from the analytical procedure.

Inherent and Control Risk

Inherent Risk (IR)

1. Inherent risk is the susceptibility of an account balance or class of transactions to misstatement that could be material, individually or when aggregated with misstatements in other balances or classes, assuming there were no related internal controls.

2. The auditor needs to assess inherent risk at the component and at the financial statement assertion/related compliance with authority objective level. This is because inherent risk can differ by component and, within each component, by financial statement assertion/related compliance with authority objective. For example, the inherent risk of the recorded cash amount actually existing may be much higher than the inherent risk that is not properly valued.

3. The auditor usually assesses inherent risk for all components and assertions/objectives. The auditor assesses inherent risk on the significant components to ensure that the audit is effective (i.e., the auditor does not under-audit the high risk areas). The auditor assesses inherent risk on the less significant components to ensure that the audit is efficient (i.e., to avoid over-auditing the low risk areas).

4. Inherent risk needs to be assessed in a hypothetical environment – the auditor needs to assume that there are no internal controls in place.

Factors Affecting Inherent Risk

5. Inherent risk factors incorporate characteristics of an entity, a transaction, or account that exist due to:

   - the nature of the entity's programmes; and/or
   - the nature of material transactions and accounts.

a) Nature of the Entity's Programmes

6. The mission of an entity includes the implementation of various programs or services. The characteristics of these programmes or services affect the entity's susceptibility to errors and irregularities and sensitivity to changes in economic conditions. In this regard the following specific conditions may indicate the presence of inherent risk:

- Programmes are significantly affected by new/changing governmental regulations, economic factors, and/or environmental factors.
- Difficult accounting issues are associated with the administration of a significant programme(s).
- Major uncertainties or contingences, including long-term commitments, related to a particular programme(s).
- New (in existence less than 2 years) or changing (undergoing substantial modification or reorganization) programmes lack written policies or procedures, lack adequate resources, have inexperienced managers, lack adequate systems to measure performance, and generally have considerable confusion associated with them.
- Programmes that are phasing out (to be eliminated within 1 or 2 years) lack adequate resources, lack personnel motivation and interest, or involve close out activities for which controls have not been developed.
- Significant programmes have a history of improper administration, affecting operating activities.

b) Nature of material transactions and accounts

7. The nature of an entity's transactions and accounts has a direct relation to the risk of errors or irregularities. For example, accounts involving subjective management judgement (that is, loss allowance) are usually of higher risk than those involving objective determinations. Specific inherent risk conditions in this regard will include:

- New types of transactions exist;
- Significant related and/or third party transaction exist;
- Classes of transactions or accounts have one or more of the following characteristics:
  - i) difficult to audit;
  - ii) subject to significant management judgement;
  - iii) susceptible to manipulation, loss or misappropriation;
  - iv) susceptible to inappropriate application of an accounting policy; and
  - v) susceptible to problems with realization or valuation.
- Accounts have complex underlying calculations or accounting principles;
- Accounts in which the underlying activities, transactions, or events are operating under severe time constraints; and

- Accounts in which activities, transactions, or events involve the handling of unusually large cash receipts, cash payments, or wire transfers.

Control Risk (CR)

8. Control risk is the risk that internal control may fail to prevent, or detect in time, material error or irregularity in account balance or class of transactions, when combined with error in other balances or classes. Some control risk is always bound to exist because of the inherent limitations of any system of internal control, whether in the system itself or in the method of its day-to-day operation and application.

9. Control risk is a function of the strength of the entity's preventive and detective internal controls. This risk is conversely related to the quality of these controls because good detective controls will help discover and lead to the correction of any errors that occur. The better the controls, the more it is possible for auditors to rely on them, with a corresponding reduction in the extent of, and/or alteration of the nature and timing of substantive audit procedures.

Factors Affecting Control Risk

In the planning chapter of this Manual, the concept of the control environment has been discussed. In this section, specific conditions that may indicate a weak control environment, and hence a high control risk are being discussed. The same analysis could be done for control procedures also.

a) Management's Philosophy and Operating Style

11. Management's philosophy and operating style encompass a broad range of beliefs, concepts, and attitudes. Such characteristics may include management's approach to take and monitor operational/programme risks, attitudes and actions towards financial reporting, and emphasis on meeting financial and operating goals. The specific factors in this regard include:

    - Management lacks concern about internal controls and the environment in which specific controls function.
    - Management demonstrates an aggressive approach to risk taking.
    - Management demonstrates an aggressive approach to accounting policies.
    - Management has a history of completing significant or unusual transactions near the year's end, including transactions with related parties.

- Management is reluctant to consult auditors/consultants on accounting issues, adjust the financial statements for misstatements, or make appropriate disclosures.
- Top-level management lacks the financial experience/background necessary for the positions held.
- Management is slow to respond to crisis situations in both operating and financial areas.
- Management uses unreliable and inaccurate information to make business decisions.
- Unexpected reorganization or replacement of management staff or consultants occurs frequently.
- Management personnel have a high turnover.
- Individual members of top management are unusually closely identified with specific major projects.
- Obtaining adequate audit evidence is difficult due to a lack of documentation and evasive or unreasonable responses to inquiries.
- Financial arrangements/transactions are unduly complex.
- Financial arrangements/transactions are accounted for in a way that does not appear to reflect the substance of the transaction.

b) The Entity's Organizational Structure

12. An entity's organizational structure provides the overall framework for planning, directing, and controlling operations. The organizational structure should appropriately assign authority and responsibility within the entity. An organizational structure includes the form and nature of an entity's organizational units. Concerning this part, the specific factors include:

- The organizational structure is inappropriate for the entity's size and complexity.
- The structure inhibits segregation of duties for initiating transactions, recording transactions, and maintaining custody over assets.
- Recent changes in management structure disrupt the organization.
- Operational responsibilities do not coincide with the divisional structure.
- Delegation of responsibility and authority is inappropriate.

- A lack of definition and understanding of delegated authority and responsibility exists at all levels of the organization.
- Inexperienced and/or incompetent accounting personnel are responsible for transaction processing.
- The number of supervisors is inadequate or supervisors are inaccessible.
- Key financial staffs have excessive workloads.
- Policies and procedures are established at inappropriate levels.
- The system for communicating policies and procedures is ineffective.
- Activities are dominated and controlled by a single person or a small group.

c) Methods of Assigning Authority and Responsibility

13. An entity's policies or procedures for assigning authority for operating activities and for delegating responsibility affect the understanding of established reporting relationships and responsibilities. The specific factor may include:
    - The entity's policies are inadequate regarding the assignment of responsibility and the delegation of authority for such matters as organizational goals and objectives, operating functions, and regulatory requirements.
    - Employee job descriptions do not adequately delineate specific duties, responsibilities, reporting relationships, and constraints.

d) Management's Control Methods for Monitoring and Following up on Performance

14. These control methods affect managements direct control over the exercise of authority delegated to others and ability to supervise overall entity activities. The specific factor may include:
    - Management is not sufficiently involved in reviewing the entity's performance.
    - Management control methods are inadequate to investigate unusual or exceptional situations and to take appropriate and timely corrective action.
    - Management lacks concern for and does not effectively, establish and monitor policies for developing and modifying accounting systems and control techniques.

f) The Effectiveness of Internal Audit

15. The following may indicate the presence of control risk:
    - The audit staff is responsible for making operational decisions or for controlling other original accounting work subject to audit.
    - Management personnel are inexperienced for the tasks assigned.
    - Training activities are minimal including little or no participation in formal courses and seminars and inadequate on-the-job training.
    - Resources to effectively conduct audits and investigations are inadequate.
    - Audits are not focused on areas of highest exposure to the entity.
    - Standards against which the auditor's work is measured are minimal or non-existent.
    - Performance reviews are non-existent or irregular.
    - The audit planning process is non-existent or inadequate, including little or no concentration on significant matters and little or no consideration of the results of prior audits and current developments.
    - Supervision and review procedures are non-existent or inadequate.
    - Working paper documentation (audit programmes, evidence of work performed, and support for audit findings) is incomplete.

f) Personnel Policies and Practices

16. Personnel policies and practices affect an entity's ability to employ sufficient competent personnel to accomplish its goals and objectives. Such policies and practices include hiring, training, evaluating, promoting, compensating, and assisting employees in the performance of their assigned responsibilities by giving them the necessary resources.

17. The following indicate specific conditions of weak control environment:
    - Personnel policies for hiring and retaining capable people are inadequate.
    - Standards and procedures for hiring, promoting, transferring, retiring, and terminating personnel are insufficient.
    - Training programmes do not adequately offer employees the opportunity to improve their performance or encourage their advancement.
    - Written job descriptions and reference manuals are inadequately maintained.

- Communication of personnel policies and procedures at field locations is inadequate.
- The channels of communication for personnel reporting suspected improprieties are inappropriate.
- Policies on employee supervision are inappropriate or obsolete.

g) Influences External to the Entity

18. Influences outside an entity's authority may affect its operations and practices. Such influences include monitoring and compliance requirements imposed by legislative bodies, general business conditions, and other economic factors. The specific factors include:
    - The functioning of oversight bodies (including Parliamentary Committees).
    - Estimates are sensitive to economic conditions affecting the entity or related entities.
    - The media has exhibited special interest in the entity or one of its programs.
    - Management's follow-up action in response to communications from legislative or regulatory bodies is not timely or appropriate.

19. When assessing the functioning of oversight bodies, the following would normally indicate that these bodies would not have a positive influence on internal control:

    - Oversight bodies demonstrate little concern toward controls and the speed with which internal and external auditors' recommendations are addressed.
    - Oversight bodies have little involvement in and scrutiny of activities.
    - Little interaction occurs between oversight bodies and the internal auditor and external auditors.
    - Oversight bodies demonstrate little concern for compliance with applicable laws, regulations, and contractual requirements.

h) Management's Control Methods over Budget Formulation and Execution

20. Management's budget control methods affect the authorized use of appropriated funds. The specific factors which indicate control weakness may include:

- Little or no guidance material and instructions are available to provide direction to those preparing the budget information.
- Management demonstrates little concern for reliable budget information.
- Management participation in directing, and reviewing the budget process is inadequate or limited.
- Management is not involved in determining when, how much and for what purpose expenditures can be made.

i) Management's Control Methods over Compliance with Laws and Regulations

21. The followings are the factors that indicate control weakness:
    - Management is unaware of the applicable laws and regulation and potential problems.
    - A mechanism to inform management of the existence of illegal acts does not exist.
    - Management neglects to react to identify instances of noncompliance with laws and regulations.
    - Management is reluctant to provide evidential matter necessary to evaluate whether noncompliance with laws and regulations has occurred.
    - Management is not responsive to changes in legislative or regulatory bodies' requirements.
    - Policies and procedures for complying with laws and regulation are weak or non-existent.
    - Policies on such matters as acceptable business practices, conflicts of interest, and codes of conduct are weak or non-existent.

j) Management's Ability to Promptly Identify and React to Changing Conditions

22. Since conditions external to and within an entity will continue to change, management's ability to identify and react to such changes can affect achievement of the entity's objectives. The extent to which such changes require management's attention depends on the effect they may have in the particular circumstances. Specific factors concerning this may include:

    - The mechanisms for identifying and communicating events, activities, and conditions that affect operation or financial reporting objectives are insufficient.
    - Accounting and/or information systems are not modified in response to changing conditions.
    - No consideration is given to designing new or alternative controls in response to changing conditions.
    - Management is unresponsive to changing conditions.

Assessing Inherent Risk and Control Risk

23. The assessment of Inherent Risk (IR) and Control Risk (CR) is clearly a subjective process requiring the exercise of professional judgement.
24. When assessing IR and CR in the planning stage, the auditor must consider each component and each financial statement assertion/related compliance with authority objective separately. This is because the risk often differs among components and assertions/objectives.
25. Because the auditor must ensure that the inherent risk and control risk are low enough to support the desired inherent assurance and control assurance for all significant error conditions, he or she must usually assess the risk for each of the significant error conditions on which assurance is being planned. This will be necessary even when the auditor subsequently decides to develop an audit strategy solely by assertion, related authority objective or by components.
26. While assessing IR and CR, the auditor should identify conditions that significantly increase inherent and control risk. When considering control risk, the auditor would consider, among other matters, identified control environment weakness.
27. The auditor identifies specific inherent risks and control risks based on information obtained earlier in the planning phase, primarily from understanding the entity's operations and preliminary analytical procedures.
28. The auditor can also consider misstatements found in previous years. If there were significant audit adjustments, the auditor may not know if the misstatements were due to there being a high inherent risk or a high control risk, but the auditor would know that the combined risk was high. Similarly, if there have been no misstatements found in previous years, the auditor would have an indication that the combined risk was low.
29. After considering his/her knowledge of the entity and factors affecting these risks, the auditor should identify and document any significant inherent and control risk in the risk analysis forms (see the risk analysis forms at Annexes D and E).
30. For each inherent and control risk identified, the auditor should document the nature and extent of the risk; the conditions that gave rise to that risk and the specific accounts, line, items and related assertions affected.
31. Finally, based on the information gathered and the factors identified, the auditor should determine the assessment of each of inherent and control risk as low or high.

    - **Low risk:** based on the evaluation of inherent risk and control risk, but prior to the application of substantive audit procedures, the auditor believes that any aggregate misstatements do not exceed planning materiality; or

- **High risk:** based on the evaluation of inherent risk and control risk, but prior to the application of substantive procedures, the auditor believes that it is likely that any aggregate misstatements exceed planning materiality. As a result, the auditor will need to obtain most, if not all, audit reliance from substantive tests.

Detection Risk

32. Detection risk is the risk that an auditor's substantive procedures will not detect a misstatement that exists in an account balance or class of transactions that could be material, individually or when aggregated with misstatements in other balances or classes of transactions.
33. This figure is used to determine the extent of substantive testing required to ensure that we have sufficient evidence to support the audit opinion.
34. Detection risk is usually grouped into two categories – analytical procedures and substantive tests of details. The latter includes 100% examinations of individually significant transactions (high value and key items), and sampling.
35. Detection risk arises partly from uncertainties that exist when the auditor does not examine 100% of transactions and balances, and partly from uncertainties that exist even if he were to carry out a 100% examination.
36. The auditor should consider the assessed level of inherent risk and control risk in determining the nature, timing and extent of substantive procedures required to reduce the assessed level of audit risk to an acceptable level. In this regard, the auditor would consider:

    - The nature of substantive procedures, for example, using tests directed towards independent parties outside the entity rather than tests directed towards parties or documentation within the entity or using tests of details for particular audit objective in addition to analytical procedures.
    - The timing of substantive procedures, for example, performing at end of period rather than at an earlier date; and
    - The extent of substantive procedures, for example, using a larger sample size.

37. For a given audit risk, there is a converse relationship between detection risk and the combined level of inherent and control risks. When inherent and control risks are high, acceptable detection risk needs to be low to reduce audit risk to an acceptably low level. On the other hand, when inherent and control risks are low (and when the auditor does sufficient tests of controls to support his/her assessment of control risk), an auditor can accept a higher detection risk and still reduce audit risk to an acceptably low level.

38. The assessed level of inherent and control risks cannot be sufficiently low to eliminate the need for the auditor to perform substantive procedures. Regardless of the assessed levels of inherent and control risks, the auditor should perform some substantive procedures on material account balances and classes of transactions.
39. The auditor's assessment of the components of audit risk may change during the course of an audit. For example, information may come to the auditor's attention when he/she performing substantive procedures that differ significantly from information on which the auditor originally assessed inherent and control risks. In such cases the auditor would modify the planned substantive procedures based on a revision of the assessed levels of inherent and control risks.
40. The higher the assessment of inherent and control risks the more audit evidence the auditor should obtain from the performance of substantive procedures. When both inherent and control risks are assessed as high the auditor needs to consider whether or not substantive procedures can provide sufficient appropriate audit evidence to reduce detection risk and, therefore, audit risk to an acceptably low level.

Illustration of the Interrelationship of the Components of Audit Risk

41. The following table shows how the acceptably level of detection risk may vary based on assessment of inherent and control risks:

Auditor's Assessment of control risk			
	High	Low	
Auditor’s Assessment of inherent risk	High Low	Medium	
	Low Medium	High	

42. There is a converse relationship between detection risk and the combined level of inherent risk and control risk.

Sampling Risk

43. Sampling risk arises from the obvious fact that only a sample is selected for the audit tests, so that items in a population falling outside the selected sample may or may not contain material error. In other words, conclusions might be reached which could have been different had the whole population been examined. That is, a particular sample may contain proportionately more or fewer monetary errors, internal control deviations or compliance with authority deviations than exist in the population. Sampling risk increases from zero as the sample size decreases from 100% of the audited population.
44. The auditor is concerned with two aspects of sampling risk when performing substantive tests of details:

- **Risk of incorrect acceptance** is the risk that the sample supports the conclusions that the population is not materially misstated even though, in fact, the population is materially misstated; and
- **Risk of incorrect rejection** is the risk that the sample supports the conclusion that the population is materially misstated even though it is not. In other words, the risk those unfavourable conclusions might be reached on the basis of a sample where as a 100% examination might have revealed no material error.

45. The latter risk is usually assumed to be negligible. Entity officials will normally not accept a qualified opinion without insisting on more work being done. This additional work will normally lead the auditor to the correct conclusion.

46. The auditor is also concerned with two aspects of sampling risk in performing tests of internal control:

- **Risk of over-reliance on internal control** is the risk that the sample supports the auditor's planned degree of reliance on the control even though the true deviation rate does not justify such reliance; and
- **Risk of under-reliance on internal control** is the risk that the sample does not support the auditor's planned degree of reliance on the control even though the true deviation rate supports such reliance.

47. As with substantive testing and the risk of incorrect rejection, the risk of under-reliance on internal control is normally assumed to be minimal. If the auditor wanted to report the weaknesses/deviations in internal control, entity officials would often insist on more work being done. The additional work would normally lead to the correct conclusion.

Non-Sampling Risk

48. Non-sampling risk is the risk that, even if the auditor carries out a 100% examination of all transactions and balances, material error or irregularity may yet remain undetected owing to human error in audit. It exists owing to factors such as inadequately trained audit staff, failure to exercise due care and diligence, inappropriate audit procedures, inadequate audit supervision etc. Given factors such as these, a much better term for 'non-sampling risk' is 'audit performance risk'.

    Because non-sampling risk is not subject to measurement and, unlike sampling risk, cannot be controlled through changes in sample size, the following precautions should be taken:

    - Test objectives and descriptions of procedures to be performed and errors or deviations to be found should be stated unambiguously.

- Auditors should be properly instructed and supervised to ensure that errors or deviations are recognized and correctly dealt with.
- Audit working papers should be carefully reviewed.

49. The auditor normally assumes that non-sampling risk (audit performance risk) is nil when the auditor complies with the Bangladesh Government Auditing Standards.

Analytical Procedures Risk

50. As noted above, auditors often divide detection risk into two components – analytical procedures and substantive tests of details. The auditor must consider the nature and effectiveness of his/her analytical procedures. As the auditor performs analytical reviews of the ratios and trends and/or additional detailed audit procedures, reliance on substantive tests of details can be reduced from what would be required in the absence of these other procedures. The auditor, therefore, can use a lower reliance level for the substantive tests of details, with a corresponding reduction in the size of sample.
51. When auditors increase reliance on analytical procedures, they should very carefully evaluate any unusual conditions revealed by any of the tests performed. The auditor cannot find an unusual condition in one test and then ignore it because the other tests fail to reveal it. The failure of any single test to reveal a condition of interest does not positively indicate that it does not exist; therefore, unusual circumstances revealed in any test require further investigation, regardless of the outcome of other tests.

Annex- J.1

Audit Programme: Records and Accounting entries of 'Payroll' of the Ministry of Fisheries and Livestock

The payments of 'pay-roll' of the Ministry of Fisheries and Livestock should be done with compliance of the existing rules and regulations and directives of the Ministry of Finance. The benefits and other facilities provided to the employees should not be inflated or undermined. Arrear claims should be paid as per regulations.

System Objective

To ensure that the payments have been made according to the existing rules and regulations and arrear claims and other benefits are duly paid off. The budget estimation for payroll has to be justified as well.

	Details of Risks	Potential Consequences
1	Payment of inflated amounts (due to wrong pay fixation).	Irregular payment made, possibility of fraud
2	Pay roll records are not maintained properly.	possibility of fraud
3	Payments are made to the employees with no assigned activities.	possibility of fraud
4	Improper appointment/ ghost employees.	Cause financial loss to government, possibility of fraud
5	Payment of undue higher scale.	Cause financial loss to government, possibility of fraud
6	Inaccurate pension payment.	Cause financial loss to government, possibility of fraud

Audit Objectives

Evaluate the main controls over the 'payroll' payment entries to ensure that:

- All the payments are made with compliance to the existing rules and regulations and the directives of the Ministry of Finance.
- Payments are approved by the competent authorities.
- All the documents and vouchers are properly kept and correctly recorded.
- Proper compilation of Accounts.
- Physical employees are paid rather than ghost employees.

'Pay roll' entries of the Ministry of Fisheries and Livestock

Auditee:	Ministry of Fisheries and Livestock.	WP Ref			
Period Under Review:	YF 2011-12	Prepared by		Date	

Audit Test	Audit assertions	Signed/date	WP Ref
Collect a detail list of pay-roll in the FY 2011 – 12 of the concerned departments and sort the list in three categories according to nature (pay-fixation, last pay certificates, arrear payments). Select random samples of size 5 from each lot (for field offices size 3) and examine the following:			
1. Determine whether payrolls are calculated accurately.	Regularity,		
2. Match gross pay with pay fixation data.	Accuracy Regularity,		
3. Determine whether allowances are calculated as per government rules.	Accuracy Regularity Accuracy,		
4. Match gross pay with audit register.	Occurrence Accuracy Regularity Regularity Accuracy,		
5. Determine whether all deductions are correctly calculated as per rules.	Accuracy,		
6. Determine whether gross pay and net pay are correctly calculated.	Classification, Accuracy, Cut off		
7. Verify whether there are evidences that arithmetic calculations have been checked.	Accuracy,		
8. Verify that an LPC is available for all cases selected.	Cut off,		
9. Ensure that total deductions are not greater than basic pay.	Classification,		

10. Re-calculate the pay fixation for each member of the sample and assess if the pay fixations have been correctly calculated, in accordance with Government Orders. 11. Select a sample of pay-bills and check the net amount of the pay-bill against the cheque amount credited against the bank in proper time. 12. Select a sample of employees and physically verify their presence/existence. 13. Payments are booked in exact code and in proper period, the total payment does not exceed budgeted amount.	Cut off, Completeness, Regularity, Accuracy		

Example Audit Programme – Funding

Funding is received from the donors and paid into the Consolidated Fund. Funding from the Centre is then sent to the field offices where it is spent.

System Objective

Funding by the donors is received in a timely manner and allocated to the correct classification/financial year and is spent in conformity with the donor wishes.

	Details of Risks	Potential Consequences
1	Funding received from a donor and allocated to a different donor	Disclosure error on face of financial statements (one donor's figure too high and another's too low). The donors are likely to spot this (embarrassing if OCAG doesn't spot it)
2	Funding received from a donor and misappropriated	As above but for one donor, illegal act, damage to reputation for GOB, donor would be reluctant to release more funds
3	Funding received and recorded at a lower amount	As per 2 above
4	Funding received and not recorded in a timely manner/ recorded in the wrong financial year	As per 1 above (can be for just one donor, or more)
5	Contribution of different donors not separately shown in FS	Donors' demand not met
6	Discrepancy between field office statements and central records (mismatch)	Accounts inaccurate, 2, 3 or 4 above
7	Closing balance and Opening balance mismatch	Accounts inaccurate
8	Discrepancy between the total resources and the total expenditure	Accounts inaccurate
9	Misleading /False disclosures	Accounts inaccurate
10	Financial Statement overstated/misstated	Accounts inaccurate

	Details of Risks	Potential Consequences
11	Arithmetic errors	Accounts inaccurate
12	Untraceable expenditure / Significant amounts remain unauditable	Accounts incomplete
13	Reconciliation of accounts not confirmed	Weakness in accounts keeping & inaccurate accounts, 2 , 3, 4 above
15	Funds are allocated and accounted for on the wrong accounts head and code	Classification of accounts not followed
16	Disbursement Link Indicators (DLIs) not achieved	Donors cease to provide funding
17	Re-appropriation made but not authorized	Accounts inaccurate

Audit Objectives for funding

The main controls over funding are to ensure that:

- Amounts disclosed in the financial statements are true and fair;
- Fund received is allocated to the correct donor and at the correct amount and in the correct financial year.
- Fund is not completely or partially misappropriated;
- Fund is spent in accordance with donor wishes;
- Fund received at the centre and all funds timely disbursed to the field offices.
- Expenditure statements from the field are timely collected and reconciled to the central accounts.

Audit Objective	Definition
Completeness	All funds relevant to the period have been recorded.
Occurrence	All amounts of funds actually occurred during the financial period.
Accuracy	All receipts of funds have been recorded at the correct value during the period.
Classification	Funds have been properly classified in the government accounts to the correct heads and codes.

Audit Objective	Definition
Cut-off	Funds have been recorded in the correct accounting period.
Regularity	Funds are treated and accounted for in line with GOB regulations and donor guidelines.

Funding

Auditee:	**Directorate of Primary Education**	**WP Ref**			
Period Under Review:	**Year ending 30 June 2013**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Audit Test	Audit assertions	Signed/ date	WP Ref
1. Obtain a listing of all funds received from each donor (directly from each donor) – obtain source of funding, amounts and dates: a) Check total and individual amounts and dates agree to the Appropriation Accounts; b) Check total and individual amounts and dates agree to draft account disclosure (including quarterly figures).	Completeness, Occurrence, Accuracy, Cut-off Completeness, Occurrence, Accuracy, Classification Cut-off		
2. Obtain a listing of projects funded from the Consolidated Fund – obtain amounts and dates: a) Check total and individual amounts and dates agree to the Appropriation Accounts;	Completeness, Occurrence, Accuracy, Regularity Cut-off Completeness,		

b) Check total and individual amounts and dates agree to draft accounts disclosure (including quarterly figures).	Occurrence, Accuracy, Regularity Classification Cut-off		
3. Obtain central records of funding amounts and dates send to field offices. Check total and individual amounts and dates agree to the Field Office statements;	Completeness, Occurrence, Accuracy, Regularity, Cut-off		
4. Obtain details of all re-appropriations. For each, check that there was appropriate level of authorisation in conformity with delegated authority limits	Regularity Classification, Cut-off		
5. Look for evidence of appropriate internal control in the area of funding, e.g. a) reconciliations of amounts of funding received from donors and GOB to accounts disclosure. b) accuracy of quarterly reporting – for one quarter selected at random check for evidence of internal control to confirm accuracy of the figures reported.	Completeness, Occurrence, Accuracy, Regularity, Classification, Cut-off		

Example Audit Programme: – Capital Expenditure, Supplies and services & Repairs and maintenance

Capital Expenditure, supplies and services and repairs and maintenance are made by the Director General (Programme Director) of Primary Education for the procurement of assets and equipment, supplies and services and repairs and maintenance.

System Objective

Procurement of bona fide assets and equipment, supplies and services and repairs and maintenance for which there is a genuine need and the amount is spent in conformity with the Public Procurement Rules and in a timely manner.

	Details of Risks	Potential Consequences
1	Expenditure for which there was no genuine need	Overstatement of capital expenditure in the financial statements and irregular expenditure
2	Fraud / Irregular expenditure / Loss of fund/Misuse	Overstatement of capital expenditure in the financial statements and irregular expenditure
3	Without approval/ Beyond DPP provision /Questionable expenditure	Overstatement of capital expenditure in the financial statements and irregular expenditure
4	Failure to fully apply the Public Procurement Rules/Violation of PPR	Overstatement of capital expenditure in the financial statements and irregular expenditure
5	Expenditure charged to the wrong year of account	Under or overstatement of capital expenditure in the financial statements
6	Expenditure authorised by an individual in excess of his delegated authority limit	Violation of delegation of financial powers
7	Expenditure charged to the wrong ledger code/in the incorrect account figure	Misclassification of expenditure in the financial statements
8	For capital expenditure, stock entry & distribution report of capital assets and equipment not confirmed	Fraud, violation of Government rule
9	For capital expenditure, quality of assets and equipment was low	Misuse of money

	Details of Risks	Potential Consequences
10	VAT/other taxes are paid where appropriate	Government deprived from revenue
11	For repairs and maintenance, payments in respect of non-project vehicles or overly frequent repairs in excess of need	Irregular expenditure
12	Risk that goods received are not of an appropriate quality and so represent bad value for money	Poor value for money

Audit Objectives for capital expenditure, supplies and services and repairs and maintenance

The main controls over capital expenditure, supplies and services and repairs and maintenance are to ensure that:

- There was a genuine need for the item/service;
- The item/service was bona fide and non-fraudulent.
- The procurement was in consistency with the Public Procurement Rules;
- The amount is charged to the correct year of account;
- The individual who authorises does so at an amount within their delegated authority limit;
- The amount is charged to the correct ledger code/account figure; and
- Taxes are paid as appropriate.
- Quality of capital assets and equipment was ensured
- Stock register and distribution reports were maintained
- Payments are not made for non-project vehicles.

Audit Objective	Definition
Completeness	All capital expenditure, supplies and services and repairs and maintenance relevant to the period has been recorded.
Occurrence	All amounts of capital expenditure, supplies and services and repairs and maintenance actually occurred during the financial period.
Accuracy	All capital expenditure, supplies and services and repairs and maintenance have

Audit Objective	Definition
	been recorded at the correct value during the period.
Classification	Capital expenditure, supplies and services and repairs and maintenance have been properly classified in the government accounts to the correct heads and codes.
Cut-off	Capital expenditure, supplies and services and repairs and maintenance have been recorded in the correct accounting period.
Regularity	Capital expenditure, supplies and services and repairs and maintenance are treated and accounted for in line with GOB regulations and donor guidelines.

Auditee:	**Directorate of Primary Education**	**WP Ref**			
Period Under Review:	**Year ending 30 June 2013**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Audit Test	Audit assertions	Signed/ date	WP Ref
1. Obtain a listing of all capital expenditure, supplies and services and repairs and maintenance in the financial year (including payee, amounts, dates and tax paid): a) Check total agrees to the Appropriation Accounts; b) Check quarterly and annual totals agree to draft account disclosure (including quarterly figures).	 Completeness, Cut-off Completeness, Classification, Cut-off		
2. Evaluate what assurance for the capital expenditure, supplies and services and repairs and maintenance account area can be taken from the high level review of quarterly outturn against budget by the Principal Accounting Officer in reports submitted to the donors.	Controls To be determined		

3. Obtain the monthly cheque reconciliation. Check 5 months including the year-end month (June). For each, check that they give assurance on whether the payments have been made accurately by the payments offices and in the correct year of account.	Controls, Accuracy, Occurrence, Cut-off, Completeness,		
4. Obtain minutes of the Ministry's monthly review meeting regarding projects. Review these minutes for anything of concern regarding capital expenditure, supplies and services and repairs and maintenance (and in such cases, if any, investigate further)	Controls To be identified		
5. For a sample of transactions from the listing used for test & check that: a) there is evidence that tender opening was done in conformity with the PPR; b) check the evaluation report was done in conformity with the PPR; c) there was a submission of a performance guarantee by the awarded bidder (where appropriate); d) the contract was made in conformity with the terms of the tender documents and the conditions of the approving authority; e) payment was within the authoriser's delegated authority limit; f) review the contract execution to ensure that the goods were received at the right amount/quality/specification and in the correct financial year (etc) by checking amount received agrees to stock and issue register, distribution register, invoice, purchase order, requisition slip (signed by authorised officer); g) check to accounting documents eg. cash book to confirm that the amount was charged to the correct year of account and charged to the correct accounts code. h) If the payment is for repairs and maintenance	 Regularity Regularity Regularity Accuracy Regularity Regularity Regularity Occurrence, Accuracy Cut-off Cut-off Classification Occurrence,		

to a vehicle, check to the log book that this is a genuine project vehicle and the amount spent agrees. i) check the bills/vouchers are genuine/authentic	Regularity Accuracy		
6. Reconcile the figures of the Ministry/DPE with those of the Chief Accounts Office (single test of relevance to all audit areas).	Completeness Classification Accuracy Cut-off		
7. Look for evidence of appropriate internal control in the area of capital expenditure, supplies and services and repairs and maintenance, e.g. a) accuracy of quarterly reporting – for one quarter selected at random check for evidence of internal control to confirm accuracy of the figures reported b) there is a evidenced system of delegation of financial authority which is observed in practice; c) there is periodic review of outturn in comparison to budget and explanations for variance are given as appropriate. d) there is good evidence of segregation of duties throughout the procurement process (e.g. different officers initiate, receipt, and authorise payment) e) there is control over changes to supplier details (e.g. change in address details) – all such changes should be properly evidenced, initiated by one officer and authorised by a different officer. f) there is appropriate review and checking by higher authorities in compliance with	Completeness, Occurrence, Accuracy, Regularity Classification Cut-off		

the PPR. NB: there should be evidence that all internal controls were in place throughout the financial year being tested.			

Annex –J.4

<u>Example of Audit Programme</u>: Training

<u>Total expenditure</u>: 8,55,51,109

Training Expenditure is made by NAPE, PTI, RPATC.

System objective

There is a genuine need of training and it contributes to the skill development.

	Details of Risks	Potential Consequences
1	Participants list was not proper	Training objectives were not confirmed
2	Training subjects were not relevant	Training objectives were not achieved
3	Participants attendance sheet was not confirmed	Loss of money, fraud
4	Procurement of training materials was not ok	Training objectives were frustrated, misappropriation
5	Distribution of training materials was not confirmed	Loss of money, fraud
6	Training honorarium/allowance was not appropriate	Violation of govt. rules
7	VAT/other taxes are not paid where appropriate	Govt. deprived of revenue
8	Training module was not prepared and followed	Improper training

Audit Objectives for training expenditure

The main controls over training expenditure are to ensure that:

- There was a genuine need for the training;
- Training was effective and result based.
- Training materials procurement was consistent with the Public Procurement Rules;
- The amount is accounted for to the correct head of account;

- The individual who authorises does so at an amount within their delegated authority limit;
- The amount is charged to the correct ledger code/account figure; and
- Taxes are paid as appropriate.

Audit Objective	**Definition**
Completeness	All training expenditure relevant to the period has been recorded.
Occurrence	All amounts of training expenditure actually occurred during the financial period.
Accuracy	All training expenditure has been recorded at the correct value during the period.
Classification	Training expenditure has been properly classified in the government accounts to the correct fund.
Cut-off	Training expenditure has been recorded in the correct accounting period.
Regularity	Training expenditure is treated and accounted for in line with GOB regulations and donor regulations.

Auditee:	**Directorate of Primary Education**	**WP Ref**			
Period Under Review:	**Year ending 30 June 2013**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Audit Test	Audit assertions	Signed/date	WP Ref
1. Obtain a listing of all training expenditure in the financial year (including payee, amounts, dates and tax paid): a) Check total agrees to the allocation; b) Check quarterly and annual totals agree to draft account disclosure (including quarterly figures).	Accuracy, Regularity Completeness, Accuracy, Cut-off, Classification		
2. Evaluate what assurance for the training expenditure account area can be taken from the high level monitoring.	Controls		
3. Obtain the monthly cheque reconciliation. Check 5 months including the year-end month (June). For each, check that they give assurance on whether the payments have been made accurately by the payments offices.	Accuracy Occurrence Cut-off Completeness		
4. Obtain minutes of the Ministry's monthly review meeting regarding projects. Review these minutes for anything of concern regarding training expenditure (and in such cases, if any, investigate further).	To be identified		
5. For a sample of transactions from the listing used for test check that: a) there is evidence that procurement was done in conformity with the PPR; b) the procurement was made in conformity with the terms of the tender documents and the conditions of the approving authority; c) Training carried out was in conformity with the	Regularity Regularity		

training module guideline d) the payment was within the authoriser's delegated authority limit; e) amount was accounted for to the correct head of account; f) amount was accounted for to the correct ledger code.	Occurrence, Regularity, Accuracy Regularity Classification Classification		
6. Reconcile the figures of the Ministry/DPE with those of the Chief Accounts Office (single test of relevance to all audit areas).	Completeness Classification Accuracy Cut-off		
7. Look for evidence of appropriate internal control in the area of civil works, e.g. a) accuracy of quarterly reporting – for one quarter selected at random check for evidence of internal control to confirm accuracy of the figures reported. b) there is a evidenced system of delegation of financial authority which is observed in practice . c) there is periodic review of outturn in comparison to budget and explanations for variance are given as appropriate. d) there is good evidence of segregation of duties throughout the procurement process (eg different officers initiate, receipt , and authorise payment). e) there is control over changes to supplier details (e.g. change in address details) – all such changes should be properly evidenced, initiated by one officer and authorised by a different officer. f) there is appropriate review and checking by higher authorities in compliance with the PPR. NB: There should be evidence that all internal controls were in place throughout the financial year being tested.	Completeness, Occurrence, Accuracy, Regularity Classification Cut-off		

Annex-J.5

Example Audit Programme: STORES AND SPARES

Stores and spares include operating stocks of cables, pole and pole fittings, meters, tools, equipment and others.

This work is documented in working paper Ref: CWE001

Audit Objective	Definition
Completeness	Stores and spares reported in the accounts is complete.
Existence	Stores and spares reported in the statement of financial position at 30 June xxxx, existed.
Rights and Obligations	DESCO have rights and obligations over the Stores and spares – i.e. that they own them.
Valuation and allocation	Stores and spares are valued and allocated correctly in the statement of financial position at 30 June xxxx.
Presentation and Disclosure	Stores have been properly disclosed and presented in the financial statements.

<table>
<tr><td>Auditee:</td><td>DESCO</td><td colspan="3">WP Ref</td><td></td></tr>
<tr><td>Period Under Review:</td><td>Year ending 30 June xxxx</td><td>Prepared by</td><td></td><td>Date</td><td></td></tr>
<tr><td></td><td></td><td>Reviewed by</td><td></td><td>Date</td><td></td></tr>
<tr><td colspan="2">Test</td><td colspan="2">Assertion</td><td>Completed by</td><td>Date</td></tr>
<tr><td colspan="2">Select a sample of stock from the stock register-
• Physically inspect the stock.
• Inspect the condition of the stock.
• If the stock has been issued since 30 June xxxx and is no longer in stock at the date of the inspection, inspect documents to prove that it was issued after 30 June xxxx.
• If DESCO has a LIFO/ FIFO policy, check that this is being followed.
Select a sample of stock purchased during the year:
Perform the following tests:
1. Obtain a copy of stock requisition order.
2. Check that there was proper approval from management for the purchase of this stock.
3. Inspect a copy of the stock delivery report to check when the stock was received.</td><td colspan="2">Existence
Valuation and allocation

Existence
Rights and obligations, Valuation and allocation</td><td></td><td></td></tr>
<tr><td colspan="2">Completeness testing of stores can be linked to the results of the testing of Operating Expenditure and Administrative Expenditure.
Were any items identified in admin or operating expenses testing purchases of stores and spares? If yes, then make sure they are also included in the Stores and spares register at 30 June xxxx.
Visit the main warehouse and physically select and note</td><td colspan="2">Completeness</td><td></td><td></td></tr>
</table>

down any 30 different lines of stores and spares. Then ask management to show these stock lines in Tally (this is to make sure that they have been included in Tally and to give the auditor assurance that Stock reported is complete). Document this work.	Completeness		
Complete the disclosure checklist to ensure that the amounts have been disclosed correctly.	Presentation and Disclosure		

Annex-J.6

Example Audit Programme - ENERGY SALES

Energy Sales represents revenue received from the billing of energy consumption, demand charges, service charge and, meter and transformer rent.

This work is documented in working paper Ref: ES001

Audit Objective	Definition
Completeness	All sales relevant to the period have been recorded
Occurrence	All sales reported occurred during the financial period
Accuracy	Sales have been recorded using the correct tariff rate and are reported net of VAT
Classification	Sales revenue has been classified in the accounts and account heads
Cut-off	Sales have been recorded in the correct fiscal year
Regularity	Sales have been generated and reported in accordance with the relevant rules and regulations
Presentation and Disclosure	Sales have been properly disclosed and presented in the financial statements.

Auditee:	DESCO	WP Ref			
Period Under Review:	Year ending 30 June 2013	Prepared by		Date	
		Reviewed by		Date	

Audit Test	Audit assertions	Signed/ date	WP Ref
1. Obtain a listing of all sales generated during the year. From the monthly summary of bills that DESCO has provided, select September xxxx, December xxxx, March xxxx and June xxxx for further testing. Obtain the report that supports this month. **Perform the following tests:** a) Check that the total of the monthly report agrees to the amount recorded in Tally for the months. b) Within each month, select one bill from each of the S&D for testing. c) For each bill check the following: (i) Agree the total figure for the month selected to the monthly report; (ii) Make sure the monthly report is prepared correctly from the Monthly Operation Data; (iii) Recalculate the bill to make sure it is calculated correctly; (iv) Confirm that the bill being tested complies with necessary rules and regulations; (v) Check whether the bill has been recorded in the correct Fiscal Year; and (vi) Check that the bill has been classified correctly as energy sales.	Occurrence Accuracy Regularity Cut-off Classification Partial completeness		
2. Perform a sample test from new connections and ensure that these amounts have also been included in Tally for FY 30 June xxxx.	Completeness		
3. Complete the disclosure checklist to ensure that the amounts have been disclosed correctly.	Disclosure		

INTERESTMENT INCOME

Total Value: **Tk.xxxxx**

Interest income is interest from Short Term deposits, Fixed Deposit receipts and interest on late payment of penalties.

This work is documented in working paper Ref: I001

Audit Objective	Definition
Completeness	All interest income relevant to the period has been recorded.
Occurrence	All interest income reported occurred during the financial period.
Accuracy	Interest income has been calculated correctly.
Classification	Interest income has been classified in the accounts and account heads.
Cut-off	Interest income has been recorded in the correct fiscal year.
Regularity	Interest income has been generated and reported in accordance with the relevant rules and regulations.
Presentation and Disclosure	Interest Income has been properly disclosed and presented in the financial statements.

Auditee:	**DESCO**	**WP Ref**			
Period Under Review:	**Year ending 30 June xxxx**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Test	**Assertion**	**Performed by**	**Date**
1. Perform a sample test from a sample of FDR/ SDR/ late payment penalties in the FY 30 June xxxx and recalculate the interest income, to make sure the FDR/ STD is authorised correctly, classified correctly and is accurate. **Perform the following tests:** (i) Inspect supporting evidence to prove that this transaction occurred. (ii) Agree the details on the supporting documents to tally. (iii) Check that the interest has been calculated correctly. (iv) Ensure that this transaction accords to rules and regulations. (v) Check that the transaction is recorded in the correct fiscal year in Tally . (vi) Check that this transaction is posted to the correct ledger code in Tally.	Occurrence Accuracy Regularity Cut-off Classification		
2. Audit team to check that where a deposit has been placed each month, that 12 months of Fixed Deposit and Short Term Deposit have indeed been recognised in tally for the year. The auditor is to do any work necessary to be satisfied that all the late penalty interest that should have been included in the fiscal year, have indeed been included.	Completeness		
3. Complete the disclosure checklist to ensure that the amounts have been disclosed correctly.	Disclosure		

Miscellaneous Income: 9. Compare the current year figure to last year and check whether the variance is within 10%. If the variance is with 10% do no more work If it is more than 10% obtain explanations for any significant variance.	Occurrence Accuracy Regularity Cut-off Classification Completeness Disclosure		

EXCHANGE RATE FLUCTUATIONS

Total Value: Tk. xxxxxx

Exchange rate is the gain or loss resulting from the translation of DESCOs transactions that are denominated in foreign currency.

This work is documented in working paper Ref: FE001

Audit Objective	Definition
Completeness	All exchange gains and losses relevant to the period has been recorded.
Occurrence	Exchange gains and losses reported occurred during the financial period.
Accuracy	Exchange gains and losses have been calculated correctly.
Classification	Exchange gains and losses have been classified in the accounts and account heads.
Cut-off	Exchange gains and losses have been recorded in the correct fiscal year.
Regularity	Exchange gains and losses have been generated and reported in accordance with the relevant rules and regulations.
Presentation and Disclosure	Exchange gains have been properly disclosed and presented in the financial statements.

<table>
<tr><td colspan="2">Auditee:</td><td>DESCO</td><td colspan="3">WP Ref:</td></tr>
<tr><td>Period Under Review:</td><td>Year ending 30 June 2013</td><td>Prepared by</td><td></td><td>Date</td><td></td></tr>
<tr><td></td><td></td><td>Reviewed by</td><td></td><td>Date</td><td></td></tr>
<tr><td colspan="2">Audit Test</td><td>Audit Assertion</td><td>Test performed by</td><td colspan="2">Date</td></tr>
<tr><td colspan="2">Select a sample of exchange transactions in the financial year ending 30 June xxxx and ensure the transaction occurred, is accurate, is classified correctly and is regular.

Perform the following tests:

1. Inspect supporting evidence to prove that this transaction occurred.
2. Agree the details on the supporting documents to tally.
3. Check that the loan was translated at the correct exchange rate.
4. Are all the other amounts in the calculation correct?
5. Ensure that this transaction accords to rules and regulations.
6. Check that the transaction is recorded in the correct fiscal year in Tally.
7. Check that this transaction is posted to the correct ledger code in Tally.</td><td>Occurrence
Accuracy
Regularity
Cut-off
Classification</td><td></td><td colspan="2"></td></tr>
<tr><td colspan="2">8. The auditor should inspect the exchange loss calculations and consider whether there are any other foreign loans or transactions denominated in foreign currency that should</td><td>Completeness</td><td></td><td colspan="2"></td></tr>
</table>

also be included, and make sure that they have been.			
9. Complete the disclosure checklist to ensure that the amounts have been disclosed correctly.	Disclosure		

ASSETS

PROPERTY, PLANT AND EQUIPMENT

Total Value: **Tk. xxxxxx**

PPE includes land and buildings, sub-stations transformers, distribution lines and vehicles.

This work is documented in working paper Ref: PPE001

Audit Objective	Definition
Completeness	PPE reported in the accounts is complete.
Existence	PPE reported in the statement of financial position at 30 June 2013, existed.
Rights and Obligations	BTCL have rights and obligations over PPE – i.e. that they own the assets.
Valuation and allocation	PPE is valued and allocated correctly in the statement of financial position at 30 June 2013.

Auditee:	**BTCL**	**WP Ref**			
Period Under Review:	**Year ending 30 June xxxx**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Audit Test	**Audit Assertion**	**Performed by**	**Date**
1. Select a sample of assets from the Fixed Asset Register. **Perform the following tests:** (i) Physically inspect the asset to make sure the assets exist (Note: if the asset has been disposed of since 30 June xxxx, inspect the disposal documents to prove it was in existence at 30 June xxxx). (ii) Check the condition of the asset. (iii) Inspect the title deeds / ownership documents to confirm that BTCL owns the asset. (iv) Select a sample from the listing of Property Plant and Equipment additions (PPE purchased during the financial year ending 30 June xxxx) and make sure the procurement process has been followed properly for each. Also check to supporting documentation to confirm that the purchase price is accurate. (v) Completeness testing of PPE can be linked to the results of the testing of Operating Expenditure and Administrative Expenditure. (vi) Were any items identified in admin or operating expenses testing that should be fixed assets? If yes, then make sure they are included in the Fixed Assets register at 30 June xxxx.	Existence Rights and obligations Valuation and allocation Rights and obligations Regularity Valuation and allocation Completeness Completeness		
2. Complete the disclosure checklist to ensure that the amounts have been disclosed correctly.	Disclosure		

Annex-J .10

Example Audit Programme

OVERALL FINANCIAL STATEMENTS TESTING

This work is documented in working paper:

Audit Objective:
To ensure that the reporting requirements for the preparation of financial statements have been followed. To ensure all the risks that were identified at the planning stage have been addressed. To document what the overall impact of the risks have been on the audit and whether there remains any impact at the completion stage.

Auditee:	**DESCO**	**WP Ref**			
Period Under Review:	**Year ending 30 June 2013**	**Prepared by**		**Date**	
		Reviewed by		**Date**	

Audit Test	**Audit Assertion**	**Performed by**	**Date**
Significant Risks			
1. Complete the tests in the Significant Risks Testing Plan (SRTP) that the audit team has written and planned to complete during field work to address the Presumed Risk of Fraud (ISSAI 240). These tests related to (i) Revenue Recognition, (ii) Journals testing, and (iii) Bias in accounting estimates.	To be specified by the auditor		
2. Have any new significant risks been identified during the audit? If so, what is the risk and what has the auditor done to mitigate and control this risk?	To be specified by the auditor		

Risk Factors 3. The risk factors were noted in the Audit Area Testing Plan (AATP). For some of them no further work was required. For others the audit team agreed to perform further work during field work stage. The audit team must refer back to the AATP and make sure that all the additional work they planned to complete during field work to address these risk factors has been completed. Make sure the work is properly documented and referenced. 4. For each risk factor identified at the planning stage, the audit team must write an update on whether the risk factor has become a significant risk. The audit team must explain whether the risk has any significant impact on the audit.	To be specified by the auditor To be specified by the auditor		
Overall regularity work 5. Review each transaction stream for new activities and obtain evidence that the activities are regular. 6. Consider whether there is evidence that the entity has breached its pay and allowances limits set by the Finance Ministry. **Laws and regulations** 7. Consider whether unusual transaction streams are within the entity's remit (i.e. is an activity that it is allowed and authorised to be engaged in). 8. Test compliance with laws and regulations that directly affect the financial statements. **For other laws and regulations** 9. Inquire of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and 10. Inspect correspondence, if any, with the relevant licensing or regulatory authorities. **Going concern** 11. Evaluate management's assessment of the entity's ability to continue as a going concern.	Regularity Regularity Regularity Regularity Regularity Regularity Presentation and Disclosure, Classification and Understandability Presentation and Disclosure, Classification and		

12. Consider whether management's assessment includes all relevant information of which the auditor is aware as a result of the audit. 13. Inquire of management as to its knowledge of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern.	Understandability Presentation and Disclosure, Classification and Understandability		
Related Parties 14. Ensure that all the related parties that we have identified are included in management's consideration of related parties. 15. Evaluate whether the identified related party relationships and transactions have been appropriately accounted for in accordance with the applicable financial reporting framework. 16. Review the related parties disclosures against the disclosure checklist to confirm that the disclosures are complete. Where the correct disclosures have been made audit any figures considered to be material to supporting documentation.	Presentation and Disclosure, Classification and Understandability		
Comparative information 17. Consider whether the results of current year testing indicate a possible material misstatement in the comparative information.	Presentation and Disclosure, Classification and Understandability		
Trial balance 18. Confirm that the audited figures for last year's accounts have been correctly posted as the opening balances in the general ledger. 19. Ensure that the Trial Balance has been correctly drawn from the General Ledger.	Presentation and Disclosure, Classification and Understandability Accuracy		

20. Demonstrate that the audit area totals reconcile to the trial balance and or draft account.	Accuracy		
Tie through of the Financial Statements			
21. Review the financial statements, including completing disclosure checklist, to ensure all required disclosures are included.	Disclosure		
22. Examine material journal entries and other adjustments made during the course of preparing the financial statements.	Accuracy		
23. Check that the accounting policies disclosed are complete, accurate and comply with the relevant standards.	Presentation and Disclosure, Classification and Understandability		
24. Confirm that all prior year comparative figures are correctly brought forward from the previous year into the draft account.	Accuracy		
25. Cast and cross cast all figures in the draft accounts and related notes.	Accuracy		
26. Cross reference all lines in the accounts to supporting audit working papers.	Accuracy		
27. Ensure the Statement of Cash Flows and supporting notes agree to supporting documentation and have been correctly prepared.	Accuracy, Presentation and Disclosure, Classification and Understandability		
28. Ensure the Statement of Changes in Taxpayers' Equity agrees to supporting documentation, corresponds to our understanding of the entity's activities in year and has been correctly prepared.	Accuracy, Presentation and Disclosure, Classification and Understandability		

Audit of non-audit area disclosures 29. Agree disclosure of auditor's remuneration to fee assessment on plan and in fee file. For consolidated accounts, ensure this includes confirming that audit fees for consolidated entities' auditors are accurate and correctly disclosed. 30. Ensure the capital commitment note is complete and accurate. 31. Ensure that disclosures are complete and appropriate for the audited body." 32. Review the analyses of receivables and payables, and assess the client's methodology for identifying the categories of balances. Ensure those balances are accurate and categorised in line with BAS requirements. 33. Review the entity's segmental analysis, ensure that it is properly prepared and any allocation between segments has been reasonably performed. 34. Confirm that new leases have been appropriately categorised and correctly disclosed in the financial statements. **Subsequent events** 35. Obtain evidence that all events occurring between the balance sheet date and the date of the audit report requiring adjustment or disclosure have been appropriately reflected in the financial statements.	Accuracy, Presentation and Disclosure, Classification and Understandability Completeness, Accuracy, Presentation and Disclosure, Classification and Understandability Completeness, Accuracy, Presentation and Disclosure, Classification and Understandability Completeness, Accuracy, Presentation and Disclosure, Classification and Understandability Completeness, Accuracy, Presentation and Disclosure, Classification and Understandability Completeness, Accuracy, Presentation and Disclosure,		

Review of other information 36. Review the annual report to ensure that it is consistent with the financial statements.	Classification and Understandability Completeness, Accuracy, Presentation and Disclosure, Classification and Understandability		

AUDIT SAMPLING

INTRODUCTION

At the early developmental stage of auditing detailed examination of all items was common. As auditees grew in size, the detailed work required increased to a level where a 100% examination became neither necessary nor practicable, nor can it guarantee 100% accuracy anyway.

A financial audit consists of obtaining evidence to form an opinion about an account. The evidence has to be sufficient, relevant and reliable. Sufficient evidence is the quantity of evidence necessary to provide the auditor with reasonable assurance that the account is not materially misstated.

The auditor has the following options open to him when deciding how much testing of a population to do. He/she will probably use a combination of all of these options while carrying out his/her audit of the whole account. The options could be to:

1. Examine all the transactions or items in a population (100% testing). 100% testing of an entire account is normally unnecessary and usually it would be impracticable anyway. However, in carrying out any test as part of the overall audit, the auditor may sometimes decide that a particular population requires 100% examination. For example, the auditor might test all the items making up a balance if the amounts were individually material.
2. Examine less than 100% of the transactions or items. Whenever the auditor tests less than 100% of the population, he/she has to select in some way the transactions or items to be examined. Selective testing procedure falls into two categories:
    a) High value and key item selection. These collectively are often referred to as individually significant transactions, and the auditor normally audits 100% of them.

       High value items are those which individually could have a significant effect on the auditor's opinion because of their monetary value.

       To arrive at the cut-off amount above which items are considered to be high value, the auditor should use a percentage of planned precision (planning materiality less the expected total errors). If monetary-unit sampling is being used, the high value amount can be set equal to the sampling interval. If MUS is not being used, the auditor could set the cut-off amount conservatively at one-quarter planned precision or less.

Key items are items that the auditor usually also wishes to examine 100% based on his/her knowledge and experience. There may, for example, be unusual items revealed by his/her scrutiny of the accounting records and statements. They may be considered especially worthy of interest because of their nature (for example, year-end adjustments).

How the auditor goes about testing key items depends on their number and materiality. As noted, he/she normally examines 100% of them but, if there a large number of similar transactions, the auditor may examine the items which are most important in his/her judgement. If those do not reveal any significant errors, the auditor may decide to sample the remainder of them.

Examining 100% of high value items and key items does not constitute audit sampling because the auditor can reach a conclusion only on the items he/she has examined and not on the whole population from which the items have been drawn. However, if the total of the remaining is insignificant, the auditor might feel justified in forming an opinion on an account balance by examining only the high value items and key items.

b) Sampling. Here the auditor employs a sampling method with the aim of drawing a conclusion about the whole population by auditing a representative sample of the transactions. The sample would be drawn from the whole population, less the individually significant items that have been examined 100%.

Thus sampling is defined as the application of an audit procedure to less then 100 percent of the item within an account balance or class of transactions for the purpose of evaluating audit evidence about some characteristics of the items (balances or class of transactions) selected in order to form or assist in forming a conclusion concerning the population from which the sample was drawn.

Clearly the auditor wants his/her conclusion, based on examining only a sample, to be the conclusion he/she would have reached if he/she had examined the whole population. To achieve this, the auditor's sample needs to have the same characteristics as the whole population. In other words, the sample needs to be representative of the population from which it has been drawn. In fact, it is impossible to be sure that a sample is truly representative of its population and there is always a risk (known as the sampling risk) that the auditor will come to the wrong conclusion about the whole population simply because he/she has examined only part of it. The auditor must therefore try to control the sampling risk through careful planning and selection of the sample. But there will always be some uncertainty which he/she must take into account when evaluating the results of testing the sample. This is true whatever sampling method the auditor adopts.

Objective of Sampling

Sampling is only one source of audit assurance. To obtain assurance with respect to the internal control system to support his/her assessment of control risk, the auditor uses review, inquiry, observation and walk-through procedures, as well as sampling. For substantive tests, the auditor also uses analytical procedures and the testing of individually significant transactions.

These other audit procedures are often more cost-effective than sampling. Therefore, on a lot of audits the auditor will first consider the assurance that he/she can obtain from these other sources of assurance, and then look to sampling to provide the required remaining amount of assurance. With this approach, the objective of sampling is to reduce detailed checking to the minimum consistent with the required level of overall audit assurance.

The auditor, of course, must not do less than is required. The portion of the population to be examined in detail must be determined and selected so that the risk of not detecting material errors, omissions and irregularities is minimized to the level that would not seriously affect the accuracy of the audit opinion.

STATISTICAL AND NON-STATISTICAL SAMPLING

Sampling methods can be broadly categorized as statistical or non-statistical. However, both statistical and non-statistical methods have the following features in common.

(a) They both require the exercise of audit judgement in planning, selecting and evaluating the sample. (The use of the term "judgemental sampling" as the opposite of statistical sampling is therefore misleading).

(b) The auditor must make sure that he/she samples from the whole population and that the population is complete.

(c) Before beginning his/her examination of the sample, the auditor should consider the audit objective of the test and define what will constitute an error.
(d) The sample should be selected without bias towards any particular items.
(e) The sample must be large enough to ensure that the risk of it being untypical of the whole population is reduced to the level that the auditor has determined to be necessary to achieve the desired level of overall audit assurance.
(f) The results of the sample test must be evaluated in relation to the whole population.

There are two basic sample selection rules:

(i) The sample conclusion only applies to the population from which it is selected; and
(ii) The sample should be representative of the population from which it is selected.

The rule in (i) applies to both statistical and non-statistical sampling and is the primary reason for what is written in (b) above – since the sample conclusion only applies to the population from which it was selected, the auditor must ensure that he/she samples from the entire population. If, for example, the auditor wants to conclude on the expenditures for the entire year, the auditor should select his/her sample from the entire year. If the sample is selected from only one or two months, say, the sample results can only be projected over those one or two months, and the sample conclusion only relates to those one or two months.

The rule in (ii) relates directly to (d) above – in order to ensure that the sample is representative of the population from which it was selected, it should be selected without any bias towards any particular item.

The auditor has a better chance of achieving (ii) (and (d)) with a statistical sample than he/she does with a non-statistical sample. When using a non-statistical sample, though, the auditor should still strive to ensure that his/her sample is as representative of the population as is possible.

Whether the auditor uses statistical or non-statistical sampling, the auditor considers the same factors when determining the required sample size, and performs the same sample evaluation. In effect, only difference between statistical and non-statistical sampling is the way in which the sample items are selected. With statistical sampling, the sample items are selected in a way that is designed to produce a sample that is representative of the population. With non-statistical sampling, the auditor does not use as rigorous a selection method as he/she does with statistical sampling.

Given the above, the main advantages of statistical sampling over non-statistical sampling are:

- Because each sampling unit has an equal and known chance of selection, there is a better chance that the sample will be representative of the population than is the case with a non-statistical sample. When expressing an opinion on financial statements, having a representative sample is very important.
- Because there is a better chance that the sample will be representative of the population, the sample results are more objective and defensible, as are the projections of those results to the population as a whole.
- It provides a direct estimate of the maximum possible error (referred to as the upper error limit (UEL).

When not using statistical sampling, the auditor normally compensates for the less rigorous selection techniques by increasing the size of the statistical sample. The auditor could, for example:

- Increase the sample size by 20% if he/she thinks that the sample is a very good approximation of a statistical sample;
- Increase the sample size by 50% if he/she thinks that the sample is a good approximation of a statistical sample; and
- Increase the sample size by 100% (double it) if he/she thinks the sample is a reasonable approximation of a statistical sample.

As noted above, when using a non-statistical sample the auditor should still strive to ensure that his/her sample is as representative of the population as is possible. To illustrate, assume that the auditor:

(i) Determines the required statistical sample size to be 40; and
(ii) Doubles it because he/she is not taking a statistical sample.

It would not be appropriate for the auditor to then select the first 80 items from the population, select the largest 80 items, etc. The auditor must still make a reasonable attempt at selecting a sample that is representative of the population from which it was selected.

BASIC CONCEPTS AND DEFINITIONS

Sampling

Sampling is the selection of a sub-set of a population. The auditor takes a sample to reach a conclusion about the population as a whole. As such, it is important that the sample be representative of the population from which it was selected

Statistical sampling

Quite simply, statistical sampling is the selection of a sub-set of a population in such a way that each sampling unit has an equal and known chance of selection.

Statistical Sampling can also be defined as an audit sampling that uses the laws of probability for selecting and evaluating a sample from a population for the purpose of reaching at a conclusion about the population.

Sampling unit

The sampling unit is the specific item of which the population is assumed to be composed for sampling purposes.

As an example, consider a population of purchases for the year. Let's assume that the purchases are recorded by cash disbursement, that each disbursement may relate to several supplier invoices, and that each supplier invoice may relate to several purchases. In this example, the sampling unit could be:

- Each cash disbursement;
- Each supplier invoice within each cash disbursement;
- Each purchase within each supplier invoice; or
- Each Tk. within each purchase.

If the auditor set individual cash disbursement as the sampling unit, the sample selection process would be much simpler than if the auditor set an individual purchase within a supplier invoice as the sampling unit. However, by setting each cash disbursement as the sampling unit, the auditor would have to audit all supplier invoices and all purchases within each selected cash disbursement.

Physical unit

The physical unit is the specific document (cash disbursement, individual supplier invoice or individual purchase, for example) to which the sampling unit is assumed to relate.

The physical unit is normally the same as the sampling unit. The primary exception is monetary unit sampling where the sampling unit is each individual monetary unit (Tk.).

Population size

The population size is the number of sampling units (cash disbursements, supplier invoices, purchases or Tk.) in the population.

The population size will vary depending on the sampling unit being used. For example, our population of purchases for the year may be composed of 16,000 cash disbursements, 30,000 supplier invoices, 70,000 purchases, and 100,000,000 Tk. Depending on which sampling unit was selected, any of these amounts could constitute the population size.

Population value

The population value is the monetary amount of the population being sampled. In the above example, it would be Tk. 100,000,000.

As discussed above, there could be individually significant transactions that the auditor wants to examine. These could be very large transactions or high risk transactions. What auditors often do is audit 100% of these transactions, and takes a sample of the remaining transactions.

To arrive at the population value for sampling purposes, the auditor needs to subtract the total value of the individually significant transactions from the total population value. For example, if the auditor decides to audit all transactions greater than Tk. 500,000 and to take a sample of the remaining transactions, the total value of the items greater than Tk. 500,000 would be removed from the population value when determining the required sample size.

Sometimes the auditor does not know the population value at the time he/she wishes to determine the sample size. For example, the auditor may wish to select a sample of supplier invoices for the year, and may wish to start auditing the transactions well before the end of the year. In this case, the auditor will have to make an estimate of the population value at the planning stage. However, should one of the “normal” sample selection approaches for MUS be used, the sample size will automatically be adjusted for any over or underestimations of the population value.

Sampling risk

Sampling risk is the chance that a sample is not representative of the population from which it was selected.

Sampling risk can result in the auditor reaching an incorrect conclusion about the population from which the sample was selected. The auditor could either incorrectly conclude that:

- The population is not materially misstated when, in fact, it is materially misstated; or
- The population is materially misstated when, in fact, it is not materially misstated.

When planning an audit, auditors normally try to control the first risk and normally do not concern themselves with the second risk. This is because, should an auditor conclude that a population is materially misstated, entity officials will normally conduct an investigation to determine if the auditor is correct. This follow-up work would normally lead the auditor to the correct conclusion.

Confidence level

The confidence level is the degree of assurance that the auditor has that the sample is representative of the population from which it was selected. This is the converse of the sampling risk.

If the auditor uses a 95% confidence level, this means that there is a 95% chance that the sample will be representative of the population from which it was selected, and that the audit results will be correct. Put another way, there is a 5% chance that the sample is not representative of the population, and therefore the auditor may not reach a correct conclusion from the results of the work.

Precision gap widening and basic precision

Planned precision is the materiality amount less the expected total errors for the financial statements as a whole.

For example:

Materiality	Tk. 30,00,000
Expected total errors in financial statements	TK. 8,16,500
Planned precision	Tk. 21,83,500

When planning a statistical sample, though, there is one other factor that needs to be taken into account – precision gap widening.

The reason why we need to consider precision gap widening is because, for each additional Tk. 1 in the most likely error, the upper errors limit (maximum possible error) increases by more than Tk. 1. Simply subtracting the expected total errors from materiality does not deal with this effect. Therefore, planned precision needs to be reduced by a further amount. This further amount is referred to as precision gap widening.

Planned precision less precision gap widening is referred to as "basic precision". It is equal to the error that could exist in the population even if no errors were found in the sample. It therefore represents the upper error limit when the most likely error is nil.

FACTORS AFFECTING SAMPLE SIZE

Many of the factors discussed above will affect the sample size, as is illustrated in the following table:

Factor	Impact on Sample Size if Factor Increases	Comments
Population value	Increase	If population value increases with all other factors remaining the same, materiality and planned precision become smaller percentages of the population value. Hence, the auditor would need a more precise estimate of the error in the population. This would require a larger sample size.
Population size	Nil, except for very small populations	For populations with less than 10,000 sampling units, the sample size may be slightly less than would otherwise be the case.
Variability of	Nil for all types of	Variability is only a factor for those types of sampling plans

Factor	Impact on Sample Size if Factor Increases	Comments
sampling units	sampling illustrated in this section.	based on a standard deviation. ACL does not support these types of sampling plans, and they are rarely used in practice.
Materiality	Decrease	If materiality increases with all other factors remaining the same, materiality and planned precision become larger percentages of the population value. Hence the auditor would not need to have as precise an estimate of the error in the population. The auditor could then decrease the required sample size.
Planned precision	Decrease	Same discussion as materiality.
Expected total errors	Increase	The expected total errors are subtracted from the materiality amount to arrive at planned precision. Increasing expected total errors decreases planned precision, which increases the sample size.
Confidence level	Increase	Increasing the confidence level means that the auditor wants to be more certain about the results of his/her procedure. The auditor will need to take a larger sample to do this.
Sampling risk	Decrease	Increasing the sampling risk is the same as decreasing the confidence level. The auditor is willing to be less certain about the results of his/her procedure, and can therefore take a smaller sample.

METHODS OF SAMPLING

Methods of sampling may vary according to whether the auditor is working in a computerized or non-computerized environment. Statistical sampling is well suited to a computerized environment, but both statistical and non-statistical can be used in a non-computerized environment.

Statistical Sampling

Non-computerized Environment

The statistical methods most applicable to a non-computerized environment are:

i) Monetary unit sampling: (MUS)
ii) Simple Random Sampling (SRS)

i) Monetary Unit Sampling (MUS)

Monetary unit sampling is the preferred method of statistical sampling for substantive tests where the auditor wishes to determine the monetary effect of the errors found. It involves considering the total value of the population as individual monetary units (e.g. Tk.) treating them as the population (e.g. total expenditure of Tk. 30,000 equals a population of 30,000 units); taking a sample from them and examining each payment which contains an element of the sample.

The main advantage of MUS is that non-statisticians find it relatively easy to use after the minimum of training. The one possible disadvantage is that, to obtain a truly statistical sample, the process requires the values of all items to be totaled cumulatively before selection is made. In manual accounting systems this could be time consuming although most systems probably include some totaling (for example totaling of individual ledger pages) which will enable manual selection to be undertaken.

Monetary unit sampling gives a higher chance or probability of selection to high valued item (units with high recorded values) and a comparatively lower chance of selection to small valued items or selection is based on the size of the units in the population.

Selecting sample items with probabilities proportional to the recorded amounts is an alternative to 'stratifying' the population by recorded amounts. This method is simpler than stratified sampling. This has made the selection technique increasingly popular in auditing practice.

Merits of MUS

1. MUS satisfies the objectives of accepted auditing standards and can easily be used within the conceptual framework of audit sampling.
2. MUS solves the problem of detecting a very small number of large misstatements by giving the larger items a much greater chance of being included in the audit sample.

This is achieved by breaking up the big, but infrequent physical units into small but frequent monetary units.

3. MUS can be applied to a combination of several account balances. Accounts can be tested together because the sampling units (individual Tk. amounts) are homogeneous.
4. The sample size is much smaller than is normally required by the variable sampling methods (those that involve the determination of a standard deviation), and should generally be smaller than that required when stratified sampling is used.

Demerits of MUS

1. Physical units that are understated have a lower probability of selection because they contain a smaller number of Tk. to be selected for sampling. Further, MUS cannot find misstatements in physical units with a book value of zero.
2. It may overstate the "true" upper error limit when a LOT of misstatements are found and cause the auditor to reject a correct client book value.

With respect to the first demerit, auditors rarely test populations to find understatements or missing transactions/amounts; rather, they examine reciprocal populations. For example, to find understatements of year-end payables, auditors would not test the year-end payable balance; rather, auditors would look at supplier invoices processed after the year-end, cash disbursements made after the year-end date, etc.

As for the second demerit, if there are a lot of errors in the sample, it is likely that the "true" upper error limit will exceed the materiality amount anyway.

Selecting an MUS Sample:

To illustrate the use of MUS, suppose the auditor is sampling a population of Tk. 100,000 expenditure balance that is contained on 500 individual payment vouchers. Instead of viewing the population as 500 different physical units from which to draw a sample, the auditor would think of the population as TK. 100,000 individual monetary units (single Tk. units) from which to draw a sample.

When an individual Tk. is selected for examination, the Tk. is not tested by itself. Instead the auditor audits the physical unit (the corresponding voucher, etc.) within which it belongs.

In applying monetary unit sampling, auditors may use a random number table or computer generated random numbers to select a random Tk. from the population.

However, systemic selection with a random start is usually recommended for its procedural simplicity. Its steps are:

1. Calculate the average sampling interval by dividing the total number of Tk. in the population by the sample size.

   $$\text{Average Sampling Interval (ASI)} = \frac{\text{Total recorded amount of the population}}{\text{Sample size}}$$

   Note: There is another formula that allows the auditor to determine the sampling interval without knowing the population value. See Annex B.

2. Select a starting point from one Tk. to the amount of the sampling interval (may use the attached random number table, Annex-Ran).

3. Set the starting point on the calculator at minus the random start.

4. Start adding the book values of each voucher until the total exceeds zero. That gets you the first sample item.

5. **From the total in (4), subtract the sampling interval to produce a negative amount. Then start adding the book values of the subsequent vouchers. When the total goes positive, that is your next sample item.**

6. **Again subtract the sampling interval to again get a negative total. (Note: The auditor may need to do this more than once if the sample item selected is more than two times the sampling interval.) Then again start adding the physical units. Continue until you have counted through the population and have the sample.**

   (Detailed illustration for MUS is presented below)

   Another sample selection method is cell selection. It combines both the systematic and the random methods. The population is divided into cells, each with Tk. equal to the sampling interval. The auditor then selects a random Tk. amount from each cell.

   This method would be very time-consuming to apply manually, but is available on IDEA.

ii) Simple Random Sampling

Simple random sampling uses random numbers to identify the sample transactions. The size of the sample is determined in the same way as for MUS. Each item in the population is given an equal chance of selection by allocating a consecutive number (for example if the total number of transaction is 1500 then each transaction can be given a number between 1 and 1500) then the required sample size is selected using random numbers.

The main advantage of this method is that it is suitable for selecting transactions which are pre-numbered and accessible in numerical order, e.g. cheques from check book stubs, and invoices filed and numbered on receipt. Its disadvantage is that it selects transactions irrespective of their value so where the transactions in the population vary in value the sample might concentrate on low value high volume transactions. For this reason it is best used for populations where the items do not vary widely in value, for example pay and pensions.

Computerized Environment

Statistical sampling may be carried out more cost effectively in a computerized environment. Both MUS and SRS are well suited to computerized environments and the comments on the methodologies described above apply.

Attributes Sampling

Introduction

Attribute sampling is used in practice to refer to three different sampling plans that are generally used by auditors to test the operating effectiveness of internal control policies and procedures by estimating the rate of deviation from proper performance. These sampling plans include:

Monetary-Unit Sampling

Monetary unit sampling is, in effect, a form of attribute sampling. (Another name given to monetary unit sampling is monetary attribute sampling.)

As noted above, monetary unit sampling produces a sample where the larger transactions have a greater chance of selection. Seeing as auditors are usually interested in monetary errors, they would usually be more concerned about internal control deviations (unapproved supplier invoices, for example) in larger transactions than in smaller ones.

The same sample selection techniques as are noted above (**random, systematic and cell) can be used for MUS for tests of controls.**

Physical attribute sampling

Physical attribute sampling is a sampling plan that is used to estimate the rate of (percentage) of occurrence of a specific quality (attribute) in a population. It answers the question "How many?" It is a common statistical sampling plan in auditing. An attribute sampling plan might for example be used to estimate the number of invoices paid twice. Attribute sampling would also help the auditor answer the question "How often". The auditor using attribute sampling might conclude "there is only a 5% risk that the true rate of double payment in the population exceeds 6% of the total population (6%x1,000) or we are 95 percent confident that, from say a population of 1,000 payments the risk of double payment would not exceed 60 (6%X1,000)."

Discovery Sampling

This is essentially the same as attribute sampling with one difference – the auditor assumes a nil deviation rate. The auditor selects the sample and, if he/she finds no deviations, then the auditor might conclude; "Since I did not observe an occurrence in the sample there is only a 5 percent risk that a payroll sheet exists in the population at a rate greater than 2 percent".

All three attribute sampling plans deal with qualitative characteristics of the population. They are used primarily by internal and independent external auditors in tests of controls when the auditor wants to estimate the extent to which prescribed internal control procedures are being followed.

These plans might be used in the following areas.

Cash Disbursement Tests: This is for occurrences where discount are not taken, invoices not properly approved, invoices are not checked for clerical accuracy, and other failure on sales posting and misstatements.

<u>Payroll Tests</u>: Apply where misstatements in hours, rates, extensions, deductions, lack of appropriate approvals or excessive vacation time occur.

<u>Inventory Tests</u>: Inventory items not properly priced, and misstatements in perpetual inventory records.

<u>Cash Receipts Tests</u>: Erroneous discounts allowed, and entries posted to incorrect accounts.

Attribute Sampling and Tests of Internal Control

In executing a test of controls, the auditor is generally concerned with the frequency of deviations from prescribed control procedures. When using attribute sampling, items being tested or evaluated must be either indicative of deviation from proper performance or not a deviation in performance. The objective of attributes sampling as it is used for test of controls or special purpose studies is to obtain a reasonable level of confidence that the population deviation rate is not beyond a certain level.

Acceptable auditing Standards require the auditor to obtain a sufficient understanding of the auditee's internal control structure to plan the audit and assess control risk. The auditor's understanding of the procedures obtained through inquiry or reference to written instructions, and an understanding of their function and limitations is based on the auditor's training, experience and judgement. The auditor's understanding of the internal control structure is documented using a flow chart, internal control questionnaire, or written narrative. Based on this information the auditor makes a preliminary assessment of the effectiveness of the prescribed internal control structures assuming that internal controls are operating effectively. At this point, the auditor may decide that it is not efficient to perform additional internal control work. Then he/she will assess control risk based solely on the evidence obtained while obtaining an understanding of the internal control structure.

If the auditor decides that it is efficient to obtain additional evidence about internal control, he/she will make a judgement about the planned assessed level of control risk, and the planned tests of controls needed to support that level of control risk. Implicit in this judgement is a consideration of the cost and benefits of the test of controls. A particular internal control will only be tested if the cost of testing the control is less than the benefit obtained from reduced substantive testing.

A judgement has to be made by the auditor about the determination of which test of controls may be performed using audit sampling. If a control is of a type that does not leave evidence of performance, audit sampling cannot be used to test its operating effectiveness.

Non-statistical Sampling

Non-statistical sampling can be defined as an audit sampling in which auditors do not utilize statistical techniques to select the sample.

As noted above, when using a non-statistical sample the auditor should still strive to ensure that his/her sample is as representative of the population as is possible. The sample selection technique should, therefore, be an approximation of a random selection, a systematic selection, etc.

As also noted above, the way in which the sample is selected is the only real difference between statistical and non-statistical sampling. In both cases, the auditor considers the same factors when determining the sample size, and when evaluating the sample results. To apply this method, auditors are expected to have sufficient knowledge about the population to justify a basis for a non-statistical sample to reach a reasonable conclusion about the population.

Merits of Non-statistical Sampling

Non-statistical sampling may be of use when the extra time required to select a statistical sample would exceed the time required to audit the extra sample items that are selected to compensate for not having a statistical sample. This could occur when, for example, selecting a statistical sample would be very costly and/or impractical.

The following table illustrates some of the factors to consider when deciding on a statistical or a non-statistical sample:

		Favours	
	Factors	Statistical Sampling	Non-statistical Sampling
a.	Set-up time		
	high		X
	low	X	
b.	Computerization		
	Yes	X	
	No		X
c.	Volume of data		
	large	X	
	small		X

There are circumstances where a purely non-statistical method of selection for representative testing is appropriate, for example, where the audited entity maintains unnumbered manual records which are not cumulatively totaled in some form. In these circumstances the auditor can apply an approximation of, say, an MUS sample using his/her judgement. In doing so, the auditor should weigh his/her sample towards high value items but ensuring that a few lower value items are selected. This can be done in several ways but two methods are:

- Quota Sampling
- Simulated MUS

Using Quota sampling, the auditor selects the sample transactions in proportion to certain characteristics in the population. For example, if 30% of the total monetary amount for all grants is in the items over Tk. 10,000 and 70% of the total monetary amount is in the items under Tk. 10,000, then in a sample size of 100, 30 transactions would be over Tk. 10,000 and 70 under TK. 10,000.

Using simulated MUS the auditor selects the sample transactions by identifying judgmentally the higher value items in the population. If the sample is selected from entries in the ledger then the auditor should select a number of ledger pages equal to the sample size (this can be done using random numbers or the higher value transaction from each pages) and take one of the higher value transactions from each page.

When sampling accounts consisting of a small number of transactions or with a small monetary value (and hence the resulting sample size would be small) the costs of applying statistical sampling may be out of proportion to the objectivity provided. In these circumstances the auditor can:

(a) calculate the required sample size for a statistical sample and increase it (as detailed below);

(b) Select a few high value transactions which amount to a large percentage of value of the account or account area; and

(c) Select the rest of the sample from the remainder of the items.

Whatever the sampling method used the auditor should document:

(a) the size of the sample and the factors which determined the size;

(b) the method by which the items were selected;

(c) the results of the tests and the most likely error for the whole population; and

(d) a conclusion about the maximum level of possible error in the whole population based upon his/her judgement and the degree of assurance with which the conclusion is formed.

Summary

The auditor designing a non-statistical sampling plan considers the same factors as the auditor designing, a statistical plan. In both cases, the auditor defines test objectives, population, sampling unit, materiality, expected total error, and confidence level. The auditor then performs the desired audit procedures on the sample and evaluates the sample results.

STAGES IN SAMPLING

1. **<u>Planning Stage (Problem Recognition Phase)</u>**

In order to plan the sample properly, the following matters need to be carefully considered:

a) **<u>Audit Objective</u>:** In planning the sample, the auditor should first identify the purpose of the audit procedures he/she wishes to perform on the sample. This would involve a consideration of the financial statement assertions and the related compliance with authority objectives and the specific error conditions, and whether a substantive test or a test of controls was being performed.

b) **<u>Population and Sampling Unit</u>:** A population is a collection of items from which a sample is drawn and about which the sample provides information. The population should be precisely defined because a conclusion based on a sample cannot be extended beyond the population to which the sample relates.

The audit objective also should be considered when defining the population. For example, if the characteristic being tested is a specific accuracy control over inventory purchases, it would not be efficient to define the population as all voucher register (purchase journal) transactions, because that population would include many items unrelated to inventory.

Because an item that has been erroneously excluded from a population to be sampled cannot be selected for testing, the auditor should perform supplementary procedures to assure that the sampled population is complete. Procedures in other phases of the audit will often provide assurance about population completeness.

<u>Defining Physical Unit</u>: As noted above, the physical unit is the element in the population for which characteristics are to be measured to estimate those characteristics for the whole population. In a substantive test, the sampling unit may be any element, provided that the value of all such elements equals the total value to be audited. If, for example, the auditor wishes to verify the total balance of accounts receivable by confirmation, any of the following could be specified as the sampling unit.

- Branch (selected branches should then be verified in total);
- Total customer balances (the usual method when using confirmation;
- Open invoices- outstanding invoices (may be more productive if customers are unable to confirm total balances and may be more efficient than total customer balances because increases in sample size may be offset by reduction in the time

required to perform alternative procedures on accounts for which confirmations have not been received, that is, non-responding accounts);

- Line items on open invoices (may be appropriate in the case of very complex invoicing procedures).

Selection of the physical unit for a substantive test should be based on considerations of convenience, economy and effectiveness, because sampling results do not depend on the level of detail (or aggregation) in the sampling unit.

Planned Precision and Basic Precision: These terms are discussed above. Planned precision represents the materially amount for the financial statements as a whole, less the expected total errors for the financial statements as a whole.

Basic precision is also discussed above. As noted in that discussion, if the auditor uses a statistical sampling software package, the software will automatically calculate this amount for the auditor.

A critical component in determining planned precision is the anticipated amount of monetary error in the financial statements. The number and magnitude of errors expected influence sample sizes because, as the number and Tk. value of errors increase, larger sample sizes are required to obtain the desired precision.

It should be stressed that, since materiality is predetermined and fixed, an over-estimation of the most likely error in the financial statements will result in a lower planned precision and a need to test more extensively in order to achieve a more tighter precision. On the other hand, under-estimation of the most likely error, while reducing the extent of testing, will normally lead to unacceptable results – the upper error limit will exceed materiality.

Error and deviations: During the design of a sample, the auditor should specify what constitutes an error or deviation, and each selected item should be evaluated according to the specifications. A representative sample provides an estimate of the characteristics in the entire population. Thus, errors or deviations in a sample should be projected to the population or stratum from which the sample was selected in order to draw an audit conclusion.

Sampling risk: Sampling risk arises from the possibility that a test applied to a sample will result in a conclusion that may be different from the conclusion that the auditor should reach if the test (audit) were applied in the same way to all sampling unit in the population. That is, a particular sample may contain proportionately more or fewer monetary errors or compliance deviations than exist in the population. Sampling risk increases from zero as the sample size decreases from 100% of the audited population.

Non-sampling Risk: Non sampling risk includes such factors as selecting audit procedures that are not appropriate for the audit objective, failing to recognize errors or deviations in documents examined, etc.

2. Execution Stage (Evidence Collection)

Determining Sample Size

The auditor should use the Sample size calculator form and Annex K.1 to determine the MUS or non-MUS sample size. However, in completing this for, the auditor should consider the additional guidance given below.

The knowledge, experience and sound judgement of the auditor is very important in determining the amount of work to be carried out during the process of the audit no matter which sampling procedure is adopted.

If the auditor decides to test items from a population, he/she needs to select the items in a logical fashion. This normally involves testing the following:

a) Those items which in his/her judgement should be examined 100%. These should include:

   i) High value items: Selection is based on the premise that if errors are to occur in the large value items, then these items should be looked at as they will be of a material nature.

   ii) Key items: These are items which require particular attention. These key items may be unusual or suspicious items revealed by scrutiny of transactions and statements or they may be considered particularly worthy of interest because of their type or may have been identified by the auditor as a weak area where transactions appear prone to error. These items will be selected entirely based on the auditor’s understanding of the inherent and control risks and the auditor’s professional judgement.

b) A representative selection of the remaining items. The auditor wants a representative selection because, if a sample is to be relied on to conclude on the population then that sample should be a good representation of the population on the whole.

The sample size when using Monetary Unit Sampling is based upon:

- the monetary value of the population;
- Performance Materiality;
- the Assurance Factor required from substantive testing; and
- whether there are any items in the population larger than Performance Materiality/Assurance Factor.

The process for testing an assertion through Monetary Unit Sampling consists of:

- determining whether it is appropriate to use Monetary Unit Sampling;
- calculating the sample size and sampling interval;
- selecting sampled items;
- performing tests of detail; and
- evaluating the results of procedures performed.

In using Monetary Unit Sampling, the expected level of error in the account as a whole, including in the balance being tested, is reflected in the Performance Materiality figure used (as this is Materiality less the anticipated level of errors).

MUS sample sizes are 50% larger for Specific Risks than for other assertions if we do not have controls assurance. It therefore may not be efficient and effective to rely upon MUS testing alone to obtain assurance over Specific Risks. Teams should consider:

- testing the operating effectiveness of controls to reduce the extent of substantive testing required;
- using Computer Assisted Audit Techniques to address the Specific Risk more precisely; or
- performing procedures to earn the right to rely upon work performed by the entity to obtain assurance over the Specific Risk.

The process for testing an assertion through Monetary Unit Sampling consists of:

- determining whether it is appropriate to use Monetary Unit Sampling;
- calculating the sample size and sampling interval;
- selecting sampled items;
- performing tests of detail; and
- evaluating the results of procedures performed.

Note - a multi-location sampling approach is generally required if transactions are processed or accounting records are held at a number of locations in such a way that a sample cannot be extracted from across the entire population. In most cases, the locations are too numerous for it to be practicable to visit them all. The sample therefore needs to be drawn in two stages ~ the number of locations to be visited, and the number of items to test at those locations. When evaluating the results the auditor needs to extrapolate the error at each location and across all locations.

Calculate the Sample Size and Sampling Interval:

The auditor should calculate the sampling interval ("SI") using the following formula:

$$\text{Sampling interval} = \frac{\text{Performance Materiality}}{\text{Assurance Factor}}$$

Where:

Assurance factor ("AF") = a factor reflecting the level of assurance required from substantive testing. As discussed in the Manual section on the Audit Assurance Model, the AF required from substantive testing reflects whether there is a Specific Risk and whether we have assurance over the operating effectiveness of controls in respect of the assertion being tested. This is a reliability factor calculated from the cumulative Poisson distribution. The value of the factor is linked to the assurance level being taken from the work:

Level of substantive testing	Assurance factor	Assurance level
Focussed	3.0	95%
Standard	2.0	86%
Basic	0.7	50%

Performance Materiality =as discussed the manual section on Materiality and Performance Materiality, this is the level of precision that we are planning to achieve around the estimate of any error identified in the population.

It is usually possible, using IDEA, to identify items greater than the sampling interval and then to select the remainder of the sample from the residual population. Where this is the case, the auditor should calculate the sample size using the following formula

$$\text{Sample Size} = \text{(Number of items greater than the sampling interval)} + \frac{\text{Residual Population}}{\text{Sampling Interval}}$$

Where:

Residual population value = the value of the set of data from which a sample is selected and about which we wish to draw conclusions, less items which are greater than the sampling interval.

Note that the sample size calculation for the residual population is equivalent to ((Residual population value X Assurance Factor)/Performance Materiality)

Excluding items greater than the sampling interval from the calculation reduces the sample size required of smaller items. If it is not practical to separate out items greater than the sampling interval, the sample size can alternatively be calculated as:

$$\textbf{Sample Size} = \frac{\textbf{Population Value}}{\textbf{Sampling Interval}}$$

Where:

Population value = the value of the entire set of data from which a sample is selected and about which we wish to draw conclusions, including any items which are greater than the sampling interval.

If we identify any additional items for testing which we consider should be included in our sample ("key items") these should also be excluded from the residual population.

Example: MUS sample size and sampling interval calculations
Population value = Tk.70,00,000
Materiality = Tk.5,00,000
Performance Materiality = Tk.3,50,000
Assurance Factor = 2.0
Sampling interval = Tk.3,50,000/2.0 = Tk.1,75,000
There are no items greater than the sampling interval, and so:
Sample size = Tk.70,00,000/Tk.1,75,000 = (Tk. 70,00,000 x 2.0)/Tk.3,50,000 = 40

Monetary Unit Sampling can result in statistically small sample sizes. This is due to the way in which the materiality is based on a consideration of the financial statements as a whole, with samples for individual balances effectively part of a wider sampling exercise for the whole account. Thus several small samples can in fact be part of a larger robust exercise across the whole account.

Statistically small sample sizes can reduce the quality of the assurance achieved, as the sampled items may not be representative of the population. To address this risk, the minimum sample size for any MUS sample is 5 items, with a minimum of 10 items when testing Specific Risks, including items greater than the sampling interval.

As noted below, if we are unable to select the sample in a systematic way, the sample size should be increased to the greater of 30 items or 125% of the original sample size.

Select Sampled items

Sampling is reliant upon the quality of the data from which the sample is selected, the sample source. The auditor should check that the sample source is suitable and that the source is a complete and accurate record of the total population to be audited.

The sample source should be tied to the trial balance and any reconciling items tested. The use of computer assisted techniques is usually an effective way to agree the general ledger to the trial balance and identify potential duplicate entries.

It is important to note that any items excluded from the sample source cannot be said to be represented in the results of the sample. Such exclusions bring bias to the sample results and this bias should be considered in the evaluation of the results of testing.

When selecting the sampled items, the auditor should ensure that where possible bias is avoided. The sample source should be examined to check for patterns in the way in which the data is stored. It may be that the records are arranged by size or that certain transaction sizes repeat on a regular basis. The auditor needs to be aware of these patterns so that the selection method remains representative of the population.

When selecting items for testing, the auditor should take into account the purpose and objectives of the audit test and should not be drawn by easily available items, interesting looking files or allow the audited body to select the samples on their behalf. The best way to ensure a statistical sample is to use a random technique, random samples can be drawn using this web link http://www.randomizer.org/form.htm, IDEA, EXCEL or random number tables.

Auditors should not attempt to guess random numbers.

If there are items which appear to be potentially of audit interest, we would usually extend the sample to include these additional “key items”, documenting why we have done so. Key items should be excluded from the residual population.

It is usually possible, using IDEA, to identify items greater than the sampling interval and then to select the remainder of the sample from the residual population on a random basis within each “cell”.

Where this is the case, the auditor should:

- select all high-value items (i.e. those larger than the sampling interval) for testing;
- divide the residual population up into "cells" using the sampling interval; and
- select an item at random from each "cell" based upon the value of the item.

An acceptable approximation to this approach can be achieved by selecting items at random within the cell without consideration of their value.

Example: Selection of items from the residual population
The residual population consists of 9 items with a total recorded value of Tk.3,300.
The sampling interval is Tk.1,100.
The residual population is divided into three cells of Tk.1,100 each and a sample of three items is selected, one from each cell.
If it is not practical to use IDEA, we may not be able to separate out the items greater than the sampling interval and select the remainder of the sample from the residual population.

However, even if "manually" picking the sample, it will usually still be practical to select the sample in the systematic way by:

- randomly generating a start-point less than or equal to the sampling interval;
- working out a cumulative total for each item within the population
- selecting items to pick by taking the start point (as a negative number), and adding the sampling interval; and
- picking items in the ledger breakdown at each of the points indicated by this calculation.

i.e. rather than picking items at random within each cell, picking the overall sample so that the items selected are randomly determined.

If using this approach, the auditor should consider particularly carefully whether there are any systematic patterns in the data set which may mean that this is approach does not generate a representative sample.

Items which are greater than the sampling interval may be "picked" more than once using this method of selecting the sample. We do not need to select additional items, but should document that this is why number of sampled items is below the sample calculation.

Example: Selection of items using a manual MUS sample

It is not possible to obtain an electronic breakdown of the balance, and so the MUS sample has been picked from a print-out. The population consists of 9 items, with a total recorded value of Tk. 3,300.

The sampling interval is Tk. 1,100, and the random start-point is Tk. 450.

Items are selected at:

-Tk.450+Tk.1,100 = Tk.650

Tk.650+Tk.1,100 = Tk.1,750

Tk. 1,750+Tk.1,100 = Tk.2,850

The next sampling interval would select an item higher than the remainder of the population, and so three items are selected for testing.

Where, due to practical reasons, it is not possible to carry out the selection using either of these methods, the sample can be selected at random within the population. However, to take account of the additional risk involved that bias may be introduced in the sample, the sample size should be uprated either to a minimum sample size of 30 or if the original sample size is greater than this by 25 per cent.

Perform tests of detail

The auditor should plan and perform appropriate tests of detail on each item selected to obtain assurance over the relevant assertions.

If a planned procedure is not applicable to a selected item, the auditor should perform the procedure on a replacement item. This item would normally be selected at random from within the same sampling interval. (Ref: ISA 530 A14)

If we are unable to apply the planned procedure, or suitable alternative procedures, to a selected item, we should treat that item as a misstatement. (Ref: ISA 530 A15-A16)

In designing the procedures to be performed, we should be clear what would count as a misstatement.

For example, in testing completeness of liabilities, a misposting between the accounts for two creditors would not represent a misstatement (although we may need to consider whether this affects other areas of our audit, including our reliance on controls).

If the selected items are not tested appropriately, this will invalidate the tests being performed. The auditor should:

- make sure that the audit test complies with the audit plan so that the responses to the tests provide the required evidence;
- test the sample item against the evidence;
- verify any discrepancies between the book value and audit value;
- gain explanations and evidence for those explanations - these must be credible and from an appropriate source; and
- record results accurately.

Evaluate results of procedures performed

The auditor should use the Error evaluation form at Annex K.2 to evaluate the errors found in the sample testing. However, the auditor should also consider the more detailed guidance given below.

The auditor should evaluate:

(a) the results of the sample testing; and (Ref: ISA 530 A21-A22)

(b) whether the test has provided a reasonable basis for conclusions about the population that has been tested. (Ref: ISA 530 A23)

For MUS sampling, this should be done by:

- assessing the impact of the nature and cause of misstatements identified;
- calculating the Most Likely Error ("MLE") and upper and lower error limits from the tests performed; and
- assessing whether the results of tests of detail provide the planned level of assurance through a quantitative assessment of the misstatements.

If we have not identified any errors in our testing, the planned assurance will have been achieved unless we have identified any other issues for consideration.

Qualitative assessment of misstatements

We should understand the nature and cause of the misstatements identified and determine whether they indicate that other misstatements may exist, including whether they impact upon other areas of the audit (Ref: ISA 530 A17).

This may be due to a previously unidentified Significant Risk.

Indications that other misstatements may exist include if a misstatement arose from a breakdown in internal control, or from inappropriate assumptions or valuation methods that have been widely applied by the entity.

If there is a risk that other misstatements may exist that, aggregated with identified misstatements, may be material, then the auditor should revise the Overall Audit Strategy and the Audit Plan.

In understanding the nature and cause of misstatements, we may identify that many have a common feature, for example, type of transaction, location, or time period. In such circumstances, we may decide to identify all items in the population that possess the common feature, and extend audit procedures to those items.

In addition, such misstatements may be intentional, and may indicate the possibility of fraud. The auditor should consider whether it is necessary to revaluate the assessed risks of material misstatement and to revise the Overall Audit Strategy and the Audit Plan.

Quantitative assessment of misstatements

If we have identified misstatements using a sample selected through Monetary Unit Sampling then we should evaluate the results of procedures by assessing whether the Upper Error Limit ("UEL") is greater than Materiality (i.e. whether the most likely error, plus additional precision, is greater than the expected error rate).

The auditor should evaluate whether we have achieved the planned level of assurance from an MUS test by comparison of the Most Likely Error + Performance Materiality + Additional Precision to Materiality.

This calculation gives us the Upper Error Limit of the misstatements identified (In other words, we have obtained reasonable assurance that the misstatements identified do not exceed the Upper Error Limit). If the Upper Error Limit is less than materiality, we accordingly have reasonable assurance that the balance is not materially misstated.

If the Upper Error Limit is above Materiality, then we may not have obtained sufficient assurance from the work performed. We should evaluate the impact on our audit and whether any additional procedures are required, as discussed below.

In addition to evaluating the impact of the misstatements identified upon the testing performed on each balance, the errors identified should be included in the Accumulation of Misstatements form for evaluation on an overall basis.

To determine the Most Likely Error, we should project misstatements found in sampled populations.

In the extremely rare circumstances we consider a misstatement discovered in a sample to be an anomaly, we should perform additional procedures to obtain sufficient appropriate audit evidence to obtain a high degree of certainty that the misstatement identified does not affect the remainder of the population.

The Most Likely Error should be calculated as:

- Most Likely Error = Known Errors + Projected Errors
- Where:
- Known errors are those from 100 per cent testing such as high value items and key items, plus any anomalous errors (i.e. those we have evidence it is inappropriate to project over the population); and
- Projected errors are the extrapolated impact of errors found by sampling. (Ref: ISA 530 A18-A20)

The Projected Errors should be calculated as:

- Projected error = sum of sample taints x sampling interval.

The sample taint is the proportion of the item in error:

- Sample taint = (Book value - audited value) ÷ book value.

For example if a Tk.14,000invoice should have been Tk 8,500, then the taint is (14,000-8,500) ÷ 14,000 = 39%.

If we have identified any errors in the testing, we should calculate the Additional Precision using by calculating the Error taints for each identified error. The table for calculating the Error taints is included in the Appendix to this Chapter. The calculation of Additional Precision is therefore:

- Additional Precision = sum of (error taint for each error x sample taint for that error) x sampling interval

Where we are testing non-significant balances, it is not necessary to calculate error taints. However, if errors are identified we should consider whether the balance is in fact non-significant.

Example: MUS evaluation of misstatements

Population being tested = Tk.10 Crore

Materiality = Tk.70 Lac

Performance Materiality = Tk.50 lac

Assurance Factor = 2.0

Sampling interval = Tk. 50 Lac/2.0 = Tk.25 Lac

There are no high value items (items greater than the sampling interval) or key items.

Sample size = Tk. 10 Croe/Tk.25 Lac = 40

Three errors were identified:

- book value of Tk. 10,000 and actual amount of Tk. 8,000, an error of Tk.2,000;
- book value of Tk.6,000 and actual amount of Tk.a 5,000, an error of Tk.600; and
- book value of Tk.5,000 and actual amount of Tk. 5,500, an error of Tk.(500).

The sample taints for these items are:

- Tk. 2,000/Tk.10,000 = 20%;
- Tk. 600/Tk.6,000 = 10%; and
- Tk.(500)/Tk.5,000 = (10%).

The sum of the sample taints is therefore 20%.

Projected error = sum of taints x SI = 20% x Tk. 2.5m = Tk.500,000

There are no high value items, key items, or anomalies so no known errors, so:

MLE = Projected Errors + Known Errors = Tk. 500,000 + Tk. nil = Tk.500,000

Additional precision for overstatements is calculated from the sum of the error taints:

- 1st error: error taint factor x sample taint = 0.75 x 20% = 0.1125
- 2nd error: error taint factor x sample taint = 0.55 x 10% = 0.0550

(Note: see appendix below for error taint factors)

Total additional precision is therefore 0.1675 x SI = 0.1675 x Tk. 25 Lac = Tk.418,750 for overstatements.

Additional precision for understatements is calculated from the error taint

- 1st error: error taint factor x sample taint = 0.75 x (10%) = 0.0750.

(Note: see appendix below for error taint factor)

The additional precision is therefore 0.0750 x SI = 0.0750 x Tk.25 Lac = Tk. 187,500 for understatements.

The Upper Error Limit for overstatements is therefore:

MLE + Performance Materiality + Additional Precision = Tk. 5,00,000 + Tk. 50 Lac + Tk. 418,750 = Tk.59,18,750.

This is below Materiality of Tk. 70 Lac, and so we have reasonable assurance (i.e. 95% confidence) that the balance is not materially overstated.

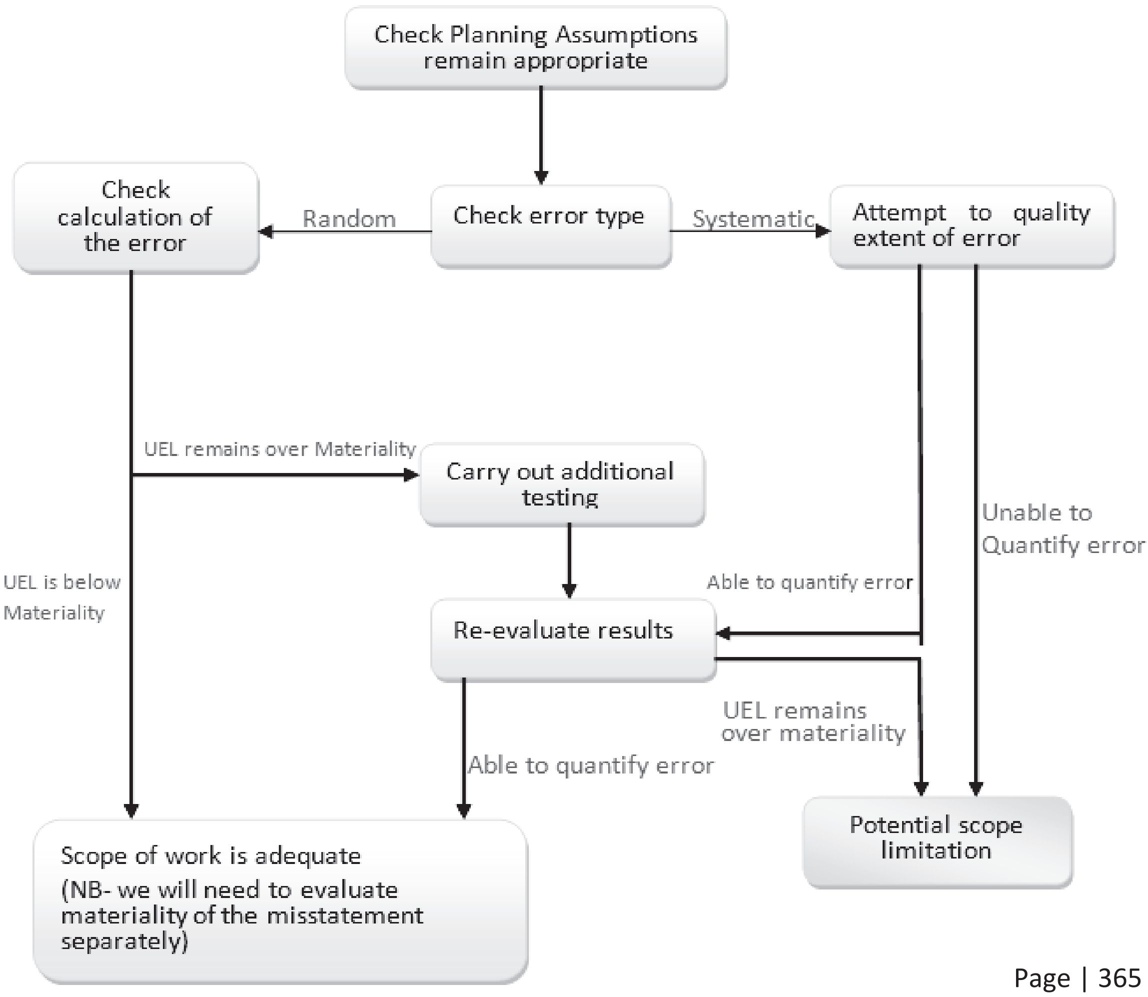
The Upper Error Limit for understatements is therefore:

- MLE + Performance Materiality + Additional Precision = Tk. 5,00,000 + Tk. 50 Lac + Tk. 1,87,500 = Tk.56,87,500.

This is below Materiality of Tk.70 Lac, and so we have reasonable assurance (i.e. 95% confidence) that the balance is not materially understated.

Responding to quantitative assessment of misstatements

If the UEL exceeds Materiality, the auditor should follow the process set out in the below flow-chart to evaluate the scope of work performed.



The process is as follows:

- Teams should consider whether their planning assumptions remain appropriate. In particular, teams should consider:
- whether the expected error rate remain appropriate, and revisit the assessment of Performance Materiality if required; and
- if we have concluded controls are operating effectively, whether this conclusion remains appropriate.

If we increase the expected error rate and reduce Performance Materiality, we should reflect the revised approach throughout the file.

- Teams should then consider whether the misstatements identified appear to be due to a systematic error, or random (non-systematic).
- For systematic errors, teams should attempt to obtain evidence enabling them to quantify the total error:

If we are able to quantify the error, then we would conclude that we have achieved the planned assurance from the test and the scope of work is adequate.

If we are not able to quantify the error, then this indicates a scope limitation to our audit.

- For random (non-systematic) errors, teams should first recheck the calculation of the error and additional precision.

If this indicates the UEL is below materiality, then we would conclude that we have achieved the planned assurance from the test and the scope of work is adequate.

Otherwise, we should perform additional testing to obtain adequate assurance.

- The auditor should assess a lower Performance Materiality for this Audit Area, and increase the extent of testing to reflect this (i.e. increase the extent of testing to that which would have been performed if we had assumed a higher error rate).
- The additional sample should be calculated as: ((Population x Assurance Factor)/(90% x (Materiality – Actual error rate)) – Original Sample.

If the additional testing reduces the UEL below materiality, then we would conclude that we have achieved the planned assurance from the test and the scope of work is adequate.

If the additional testing does not reduce the UEL below materiality (due to additional errors being identified), then this indicates a scope limitation to our audit.

Compliance Audit

Monetary Unit Sampling can be used in testing compliance with authorities (the regularity assertion).

Although it is often appropriate to test a number of assertions including regularity through MUS testing, auditors should consider whether there are more effective and efficient ways to obtain assurance over each assertion.

In particular, if Substantive Analytical Procedures would provide sufficient appropriate audit evidence over other audit assertions, but not over regularity, it may be appropriate to design an alternative approach to obtaining regularity assurance rather than testing several assertions through MUS testing.

Example: obtaining assurance over regularity and other assertions separately

Due to the nature of the entity's staffing and pay arrangements, substantive analytical procedures are an effective basis for obtaining assurance over occurrence, completeness and accuracy of payroll expenditure (with partial assurance over cut-off, with additional comfort from a direct test of the year-end cut-off of timesheets).

Regularity assurance is obtained by checking that:

- the pay awards agreed as part of the pay round were in line with the pay remit; and
- no irregular types of activity by the entity have been noted.

IT considerations

It will usually be most efficient to obtain an electronic listing of the population in order to perform MUS testing. Before selecting sample items to be tested, auditors should first ensure that this listing is reconciled to the amount(s) included in the draft account or trial balance, and test any reconciling items.

Documentation of MUS

There are no specific documentation requirements for Monetary Unit Sampling. The work performed should be documented in sufficient detail to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed and their results.

Documentation should usually include:

- the total value of the population;
- the source of the listing used to generate the sample;
- the calculation of sample sizes, including sampling interval;
- the random start point used to generate the sample;
- any further details relevant to understanding how sampled items were selected;
- the tests performed on sampled items and how these address each assertion;
- the results of the tests performed; and
- our investigation of the nature and cause of misstatements or irregularities and evaluation of their impact.

Quality and reviewing guidance

MUS testing can be a simple and effective way of obtaining assurance over assertions. However, this is dependent upon the tests performed addressing the risk we want assurance over.

If we do not perform tests on each sampled item to address an assertion, we do not obtain assurance over that assertion.

Example: Obtaining assurance over freehold property through MUS tests

The client has a large number of premises, and we are testing freehold land (which is not depreciated) using MUS sampling to obtain assurance over existence, rights and obligations, and valuation and allocation. In order to obtain assurance over each of these assertions, the items selected each need to be tested in order to check:

- for existence, that the land in question in fact exists by visiting the site (or other checks);
- for rights and obligations, that the land belongs to the client by checking the title deeds; and
- for valuation and allocation, that there are not indicators of impairment, that the revaluation has been appropriately calculated, and that the item is appropriately categorised.

Other procedures will be performed to obtain assurance over completeness.

Without performing each test, we would not obtain assurance over each assertion. E.g. without checking the title deeds (or another relevant test) we would not get assurance over rights and obligations.

Representative Sample selection Methods

After determining the sample size the auditor should select a representative sample from the population (i.e. the characteristics of the sample should not be expected to differ from those of the population except for the impact of sampling risk).

Among the possible sample selection methods the auditor can use are:

a) Simple Random sampling

A selection method whereby sampling units in the population are consecutively numbered and the sample to be audited is determined by random number table, lottery or computer (i.e. is a sample in which each sampling unit has an equal, non-zero probability of selection each draw.)

The most widely used method of simple random sampling is the random number table. The random number table can be identified by referring to the name of the table, the page number, row number and column number.

Steps in using random number table:

i. determine the range of vouchers or monetary value to be sampled in order to obtain the number of digits required.

ii) find starting point in the table; open a page and place your pencil somewhere on the table, use the digit nearest the pencil point as starting digit.

iii) proceed in a predetermined order down the column or across the column select numbers of sufficient digits unit required sample size have been drawn.

b) Haphazard Sampling

Haphazard Sampling is a sample consisting of sampling units selected by the auditor without any reason for including or omitting particular items. It is, in effect, an approximation of a random sample.

c) **<u>Systematic Sampling</u>**

Systematic sampling involves the sequential numbering and arrangement of all items in the population in serial order, and subsequent selection of the number of items required for the sample by drawing every 'K' item from the population. It is a method by which every 'K' sampling unit is selected after a random start.

Systematic selection for MUS is illustrated above. For physical attribute sampling, it can be done as follows:

i) determine the sample interval

$$\text{Sample interval} = \frac{\text{Population}}{\text{Sample size}} = K$$

ii) determine the starting point between 1 and K (the sampling interval). This is often done selecting a random number between 1 and K.

iii) add K on the starting number to get the second item to be included in the sample

Ex. suppose a sample of 300 items from a record containing 18,000 items is going to be drawn.

$$\text{sample interval} = K = \frac{18000}{300} = 60$$

If the random starting point is 48, the sampling units to be included in the sample are 48, 108, 168, 228, and 288.

<u>Remark</u>

1. In case K is not an integer, we round it down. For instance if K=60.5, it will be taken as K = 60.
2. The actual sample size may differ from the designed by one or a little more, depending on the value of K and the element selected first, but this difference is negligible when the sample size is reasonably large. For instance, if we want to select 3 items from 20, we get K=6.6 6. If the random number between 1 and 6 is 5 then the 5^{th}, 11^{th}, and 17^{th} are the ones to be selected. If the selected random number is 1 we might have selected the 1^{st}, 7^{th}, 13^{th} and 19^{th} or four items.
3. Even though the application procedures are easy, there is a slight risk that it may produce a biased (unrepresentative) sample. This could occur, for example, if the population itself has some order to it, and

the sampling interval matches that order. For example, let's say that we are auditing payroll and the division is structured as follows:

a) Each supervisor has a staff of 6 reporting to him/her;

b) The payroll records list the supervisor first, followed by his/her staff, followed by the next supervisor and his/her staff, etc.

If the sampling interval was "7", the auditor would have a sample that contained only supervisors (if the random start was 1) or no supervisors (if the random start was 2 to 7).

The risk of this happening is, of course, very small – the sampling interval would need to exactly match the pattern in the population. Furthermore, if MUS was used, the risk of this happening would be virtually zero because, in the above example, the total payroll for each division would need to match the sampling interval. If, though, the auditor was concerned about it, he/she could use more than one random start.

4. Do not substitute one sample item for another (unselected) population item. (In general, population items that are not selected should not be substituted for sample items that are difficult to audit or locate.) Instead, the auditor will normally try to find other ways to verify the existence, measurement, etc. of the unlocatable item and, if he/she is unable to do so, the auditor normally assumes that the item is in error by 100% of its recorded (book) value.

d) <u>Block sampling</u>

This method involves selection of items in a given block or sequence. Thus, the auditor may decide that he/she will examine all debtors whose names begin with the letter 'D' or he/she may decide that he/she will select all transactions of a particular month.

This is actually not a sampling method at all. The reasoning is as follows:

- As noted above, a sample conclusion only applies to the population from which it is selected. In our first example above, the population not all debtors; it is only the debtors whose names begin with the letter 'D' – there is no chance for debtors with names beginning with any other letter to be selected. Similarly, in the second example, the population is not the whole year; it is only the one month – there is no chance for transactions in other months to be selected.

- We have not "sampled" from the populations from which the transactions were selected – we've selected 100% of the transactions.

In addition to being defective because the sample is virtually never selected from the population on which the auditor wishes to reach a conclusion (all debtors or the entire year in the above examples), it also may not be efficient because it may result in more transactions being selected than would be required under a representative sample. For example, if all transactions in one month are selected, the auditor will likely have selected somewhere around one-twelfth of the transactions for the year. A "typical" statistical sample size would be much smaller.

Given the above, block sampling is not recommended for routine use. The only times when its use should be considered are when, for example:

- It would be extremely difficult or time-consuming to select a representative sample from the entire population on which the auditor wishes to reach a conclusion; and
- The auditor can, through procedures other than his/her sample, reach a conclusion with respect to the rest of the population on which he/she wishes to reach a conclusion. These other procedures could include, for example, analytical procedures.

e) Stratified Random Sampling

A stratified random sample is obtained by drawing simple random samples from separate strata in the population. The primary purpose of stratification is to bias the sample towards the larger monetary amounts.

Given this primary purpose, stratification is not necessary when MUS is used.

That is because MUS automatically biases the sample size the larger monetary units. MUS is, in effect, an infinite form of stratification.

When physical attribute sampling is used, there is no bias towards the larger monetary amounts. Therefore, stratification may be used with physical attribute sampling in order to so bias the sample items.

Stratification may also be used to:

- Achieve some efficiency by grouping sampling units with similar characteristics into separate strata.
- Get estimates of the parameters of each stratum (separate estimate) instead of a population estimate at large.

The first step in carrying out a stratified sample is to divide the population into strata that are mutually exclusive sub-populations.

These strata have to be:

- Non-overlapping (that is, every element must belong to one and only one stratum).
- Different from each other but relatively homogeneous within a stratum with regard to the measurement of interest (the logic behind to this is that, if we know the population items are virtually homogenous, we need only a small sample to describe them).
- Such that the exact number of elements in each stratum must be known.

In stratified sampling, we stratify the population and draw samples from each. We then derive the estimates from them separately, then combine these estimates to cover the whole population provided the above conditions are fulfilled. The basis for stratifying the sampling units must be among the items of information on the record, such as recorded amounts, type of item, storage location (for goods) or volume of activity based on time and cost.

In choosing among these possibilities, the auditor considers the following:

- What basis will be most efficient?
- what basis will be least expensive to implement?

Stratification

When stratifying the sampling units the auditor must choose:

The number of strata

The location of stratum boundaries

The method of allocating the total sample to the strata.

Number of Strata

There are no restrictions on the numbers of strata in the sample design. However, as a practical matter, unless the strata are clearly distinct from one another, little gain is made after a division into six strata.

Stratum Boundaries and Formations

The auditor can select the stratum boundaries as desired. If logical division exist in the population, they can be used (e.g., product line, type of item, location, and geographic areas).

In stratifying population, the first step is to decide on the non-sampled stratum (i.e., those to be examined 100%). Some auditors, as a rule of thumb, take those transaction items whose monetary value exceed one quarter of planned precision, or use what would be the sampling interval if MUS was used.

One useful approach is to select stratum boundaries so that each stratum contains approximately the same total Tk. (monetary) amount (except the 100 percent checked or non sampled stratum). To use monetary stratification, the total population amount is reduced by the 100 percent stratum amount and the remainder amount is divided by the desired numbers of strata. This yields the target total Tk. amount for a single stratum. The stratum boundaries are then selected so that each stratum has nearly the desired monetary amount. Usually four to six strata, including the 100 percent stratum is reasonable.

In defining strata and their boundaries, consideration must be given to the cost (implementation expense) and benefit (effectiveness of the test). From a cost perspective, recorded book amounts are widely used as a basis for population stratification. If possible, manual stratification of a very large population should be avoided, because it is time consuming and expensive.

Appendix: Error tainting factors for monetary unit sampling evaluation

Level of Testing	Focused	Standard	Basic
Assurance Factor	3.0	2.0	0.7
Errors			
1st	0.75	0.50	0.00
2nd	0.55	0.38	0.00
3rd	0.46	0.30	0.00
4th	0.40	0.28	0.00
5th	0.36	0.23	0.00
6th	0.33	0.23	0.00
7th	0.30	0.21	0.00
8th	0.29	0.19	0.00
9th	0.27	0.18	0.00
10th	0.26	0.18	0.00

Where we are testing non-significant balances, it is not necessary to calculate error taints. However, if errors are identified we should consider whether the balance is in fact non-significant.

Sample size calculator form

MUS Planning Form		
Account		
Account area		
Population Value		
Assurance factor		3.0
Materiality		
Anticipated error		
Safety percentage		90%
Performance materiality		-
Estimated sample size	**Number**	**Value (TK.)**
Total population value		-
Less: High value items		
Less: Key items		
Represented population		-
MUS sample size	**-**	
Total sample size	**-**	
Average sampling interval	**-**	

Instructions

Put the relevant account information into the yellow cells, the remaining cells are automatically calculated.

Average Sampling Interval (ASI) - is used to equally divide the population to allow the selection of one item from each interval

Warning - A warning will appear if the ASI is above materiality as this would mean that any 100% errors would breach materiality.

Uplift to sample size when not picked using MUS

In some circumstances, it may not be possible or practicable to use MUS sampling to select a sample of recorded amounts. If that is the case, expand by clicking on the + symbol and complete the below to calculate the sample size.	
Uplift to sample size	25%
High value items	-
Key items	-
Uplifted sample size	**-**
Revised total sample size	**-**

Sample error evaluation form

Audit area	
Total Population Value (TK.)	
Total Population Size	
High Value and Key Items Value (TK.)	
Number of High Value and Key Items	
Represented Population Value (TK.)	
Represented Population Size	
Materiality	
Anticipated Error	
Performance Materiality	
ASI	
Assurance Factor	3.0
Confidence Level	
Total Sample Size	
Random Sample Size	

Instructions

1. Input account information into the **yellow** cells only.

2. Proceed to the *Data* sheet.

Warning - A warning will appear if the ASI is above materiality as this will mean that any 100% errors will breach materiality.

Information- If additional testing has been carried out, both performance materiality and the ASI should be recalculated to reflect this.

Annex- L

LEAD SCHEDULE TEMPLATE

Instructions

The Significant Risks Testing Plan and Audit Area Testing Plan sets out the risks and testing approach for each audit area.

This form is designed to summarise our understanding of the nature of and movements in the audit areas for the year, that the testing plan has been completed, any audit adjustments identified, the final accounts figures, and any management letter points identified.

The form can be used to satisfy the requirements of the Audit Conclusions Tests in each audit area.

Also included is an issue log sheet, on which all of the individual issues for the audit area in question.

Auditors may find this useful to keep track of all of the errors that are found on each audit area.

Lead Schedule

LEAD SCHEDULE for:

Link to Testing Plan for Audit Areas:

Audit Areas	Draft Account Figure	Link to Trial Balance	Prior year final account figure	Movement on prior year	% movement on prior year	Comments on current year balance and movements	Have there been any changes to Testing Plan?		Have we completed our planned testing and assessed, quantified and extrapolated any errors?	Total Adjustments	Final Account Figure	Link to Final Accounts	Unadjusted Errors	Management Letter Points
Insert Audit Area(s) (items with similar nature, risks and controls) (should match list in Audit Area Testing Plan)	TK. '000s	Hyperlink to TB	TK. '000s				(Including identification of new Specific Risks) If yes, document reasons for changes and update Audit Area Testing Plan and/or Significant Risks Testing Plan as appropriate			Calculated from Issues Log	TK. '000s	Hyperlink to Final Accounts	Calculated from Issues Log	(Hyperlink)

Totals	-		-	-	-					-	-		-	
										Ok			Ok	

Overall Assessment
Have we obtained sufficient assurance to support the true and fair opinion?

Is the audit area free from material misstatement (either through error or irregularity)?

Have all unadjusted errors been assessed and extrapolated?

Have we obtained sufficient assurance to support the regularity opinion?

Please add comments/explanation below, if appropriate.

Disclosure Notes
Provide details of associated disclosure notes eg note reference and hyperlink to testing.

Issues Log

ISSUES LOG for: Income & Contributions in Kind

Audit Area	Financial Statement Note Line	Issue (narrative + link to exception)	Financial Error/ Disclosure	Correcting Entry	Other Financial Statement Note Line and Audit Area	Adjusted or unadjusted	Total of adjusted items	Total of unadjusted items
	Insert Note line	Provide details of the issue	Select error type	Enter the necessary correcting journal for this account area (Enter Dr's as +ve and Cr's as -ve)	Enter the Audit Area and related Financial Statement Note Line for the other side of the correcting entry - this could be more than one area.	Enter status of the error		
							-	-
							-	-
							-	-
							-	-
							-	-
							-	-
Total				-			-	-

Controls Testing

1. If we are able to obtain assurance over the operating effectiveness of appropriately designed and implemented controls, this reduces the extent of our substantive procedures. Controls tests are audit procedures designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements.

2. Using controls testing is often the most effective way to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement. Controls are never completely infallible and hence we are always required to perform substantive testing in addition to tests of controls.

3. Although we are not responsible for the system of internal control, we are able to play a valuable role in advising on improvements to the existing system of internal control identified through our tests or from comparison with other entities.

4. As controls testing reduces the scope of substantive procedures, it is important that we are clear how the controls being tested provide assurance over each assertion that we are relying on them for, and that we have appropriate evidence to support our conclusion that the control would prevent or detect a material misstatement.

5. As has been explained in the section on Audit Planning, in the course of the planning process, we should identify the controls which we plan to rely on in our testing, and obtain an understanding of them by evaluating their design and implementation. (Ref: ISA 315 A66-A68)
6. The auditor's assessment of the risks of material misstatement is informed by our understanding of the control environment. An effective control environment may allow the auditor to place more reliance on internal controls and upon the reliability of audit evidence generated within the entity itself. If there are weaknesses in the control environment which management cannot overcome the auditor would normally seek more extensive evidence from substantive testing.
7. The process of understanding the entity’s internal control and planning where to rely on controls may be an iterative process, with our conclusions about the wider control environment leading us to re-evaluate our approach to controls. E.g.:

- we planned to rely on controls over accruals, and evaluated their design and implementation. However, we concluded that weaknesses in the general control environment indicated that we should not plan to rely on any controls in this organisation;

- we may plan to test a Specific Risk substantively, evaluate the design and implementation of relevant controls, determine that they are adequately designed to prevent or detect material misstatement, and decide to plan to rely on their operating effectiveness; or

- we may not initially plan to rely on controls to test expenditure, but from our general understanding of the entity's internal control may determine it would be appropriate to do so, and evaluate the design and implementation of expenditure controls before going on to test their operating effectiveness.

8. At the audit assertion level, the auditor should ensure that the proposed audit procedures are responsive to the assessed risks of material misstatement or material irregularity. In designing the audit procedures, including deciding whether to rely upon the operating effectiveness of controls, the auditor must have regard to:
   - the significance of each risk;
   - the likelihood that a material misstatement or material irregularity will occur;
   - the characteristics of the transactions and balances; and
   - the nature of the specific internal controls (in particular, whether they are manual or automated).

Evaluation of design and implementation of controls

9. Where we are planning on relying on the operating effectiveness of a control, we should:

   - identify the Audit Areas and assertions which we are seeking to rely upon controls over;

   - for each assertion, identify the control activity or control activities that we are planning to test;

   - understand what the policies and procedures involved in the control activity are, including:

     - the individuals involved in the process
     - how exceptions, misstatements or unusual items should be handled, and whether any have arisen in the year

    - if the control is dependent upon underlying IT controls (e.g. depends upon a system generated report) and how this relates to IT controls;
    - whether there are instances where the control activity has operated inappropriately; and
    - whether there have been any modifications to the control activity in the period.

- evaluate whether the control appears to be appropriately designed, including whether it is sufficiently precise to prevent or detect material misstatements;
- identify what characteristics would indicate adequate performance of the control, and what conditions would indicate deviations from adequate performance of the control;
- test an item to see that the control has been implemented as designed; and
- evaluate the implementation of the control.

10. We should also consider whether the control is dependent upon other controls (indirect controls), and, if so, whether it is necessary to obtain audit evidence that the indirect controls are appropriately designed and implemented (and then test their operating effectiveness). (Ref: ISA 330 A30-A31)

Example: Precision of a management control

11. The entity has a monthly management accounts process. The results for the year to date are compared to budget, and variances of over 5% are investigated and reported upon to the board, which reviews the management accounts. As only variances over 5% year-to-date in aggregated data are investigated or reported upon, the Engagement Team concluded that this is not sufficiently precise to prevent or detect material misstatements
12. If the control is adequately designed and implemented, we may continue with the planned approach of testing its operating effectiveness.
13. A control is appropriately designed if, possibly in combination with other controls we have assessed, it is capable of either preventing or detecting and correcting material misstatements effectively.
14. A control is appropriately implemented if it exists and it is being used by the entity.
15. If the entity has used substantially different controls at different points in the period, we should evaluate each of them separately if we are seeking to rely on the operating effectiveness of controls throughout the period.

16. We can evaluate the implementation of controls through similar types of procedures to tests of the operating effectiveness of controls, or through walkthroughs. The types of procedures performed may include:

    - inquiry of entity personnel (coupled with other procedures);
    - walkthroughs;
    - observing the operation of a specific control; or
    - inspecting documents and reports.

17. Walkthroughs involve following one or more transactions through the accounting system and its controls to confirm the auditor's understanding of the controls, to help them to document the accounting process and provide an indication of how the controls operate in practice. Walkthroughs are particularly useful where the auditor is concerned with controls over individual transactions.
18. Depending upon the reasons, if the control is not adequately designed and implemented, we may conclude that we need assurance over the operation of a complementary or alternative control to achieve assurance over the assertion, in which case we should evaluate the design and implementation of the other control as well.
19. Alternatively, we may conclude that a controls approach is inappropriate to testing that assertion.
20. If we identify controls which are not adequately designed or implemented, including where a control that we would expect is absent, we should consider whether this has an impact upon our assessment of the risks of material misstatement. We should also report the control deficiency to management.
21. For example, if we evaluated the design and implementation of controls over purchasing and identified that there was no segregation of duties between creating suppliers on the system, inputting orders, or processing payments, in addition to assessing the design of controls as inadequate, we may identify a Specific Risk of fraud.
22. Control procedures may be classified as:

    - preventative controls, which aim to prevent misstatements arising; or
    - detective controls, which aim to identify misstatements and correct them.

23. Controls may also be classified as:

    - transaction level controls, which operate around the initiation and processing of transactions; or

- monitoring controls, which operate by considering e.g. reports of results, or by monitoring that transactional level controls have operated as expected.

24. Monitoring controls are generally detective in nature, and transactional controls are generally preventative in nature.

Example: Types of controls

25. The following are examples of controls falling into the different classifications:

    - All invoices must be approved by a department head prior to payment. The invoices are signed off by the department head and checked by the AP clerk prior to processing. This is a preventative transactional control.

    - Prior to the processing of the payment run, the Financial Controller reviews a sample of items in the batch to see that the sign-off has occurred. This is a (low-level) preventative monitoring control which checks that the transactional control has operated effectively.

    - Central finance check a sample of transactions for proper authorisation throughout the purchase to pay cycle each month. This is a detective monitoring control.

26. Where there are multiple controls which address a control objective or risk, we would normally evaluate detective or monitoring controls in preference to preventative or transactional controls, provided that they address the control objective or risk with sufficient precision to detect and correct a material misstatement.

27. Examples of types of control include:

    - High level monitoring controls, such as a regular critical review of management accounts against an appropriately detailed budget, risk based reviews of operations by management, the use of directors' statements on the state of their risks/controls and other performance data.

    - Organisational controls, which derive from the way in which the organisation is structured and can be both detective and preventive. They will normally include well-defined responsibilities and the segregation of incompatible functions such as the initiation, processing and recording of transactions.

    - Authorisation controls, which will normally operate at the individual transaction level and will be preventive in nature. Their purpose will be to stop a transaction being processed if it has not been approved at an appropriate level. Good authorisation controls will be specific about who can approve what, the extent of checking required before approval and how the check should be evidenced.

- Operational controls, which are concerned with the completeness and accuracy of processing and may be either preventive or detective. They may include comparison of one set of documents to another (e.g. purchase orders to invoices); and the use of control totals and reconciliations.

- Physical controls, which are usually designed to be preventative and include controls over access to assets and accounting records through simple physical measures such as passes and safes but also logical controls such as password access to computer files.

28. Further examples of the types of controls we would expect to see in respect of particular risks are set out below:

    - Transactions governed by complex regulations. Mitigating controls might be based on the use of procedural manuals and management re-performance or review of transactions to check compliance;

    - Functions carried out at a number of different locations. Mitigating controls could address risks of weakened management control or of inconsistencies between the locations. Controls might include budgets and outturn comparisons within each location and between locations and checks to ensure that procedural manuals and supervisory arrangements are followed;

    - Transactions based on claims or certificates from external parties. Mitigating controls could include established criteria for claims, standard requirements for evidence to support claims and independent verification;

    - Transactions not in the normal course of business. Mitigating controls might be the production of exception reports and documented follow-up actions, and senior management/board authorisation;

    - Accounting estimates. Mitigating controls might include management or independent reviews of the basis of the estimates and checks on supporting documentation; and

    - Period-end adjustments. It is possible to introduce a material error with an accounting adjustment, even though the control procedures have operated effectively up to that point. Mitigating controls might include detailed checking and management review of supporting documentation for accounting adjustments.

29. Where controls we plan to rely upon are dependent upon general IT controls, we should consider the procedures we need to perform over IT controls, as discussed further below.

The effect of testing internal controls on our audit approach

30. If the entity has strong internal controls, tests of controls may provide assurance over any assertion or Audit Area.

31. However, the most effective and efficient approach to testing will depend on the relative difficulty of testing controls and performing substantive tests, which is affected by:

    - whether a limited number of controls provide assurance over multiple assertions and Audit Areas; and
    - the size of particular balances and so sample sizes if performing tests of detail.

32. We should obtain more persuasive audit evidence the greater the reliance we are placing on the operating effectiveness of the control. (Ref: ISA 330 A25)

33. Accordingly, where we are planning to rely on controls that address Specific Risks, we should obtain more persuasive evidence by varying the nature, timing and extent of our procedures.

34. No control system can guarantee proper administration and the completeness and accuracy of transactions. We cannot, therefore, obtain all audit evidence solely from controls. In evaluating and testing controls, the Engagement Team should be aware of these limitations and the factors that may diminish the effectiveness of control systems, such as:

    - the precision with which the control may be expected to operate (i.e. if comparing to a budget, how much volatility would be expected anyway, and so how small a misstatement may be identified);
    - the potential for controls to be overridden by those responsible for them;
    - improper application of controls due to human error as a result of mistaken judgement or interpretation, carelessness or distraction;
    - the inability of standardised control systems to deal with non-routine transactions; and

- control breakdown due to changes in processing transactions and the development of non-standard procedures.

35. We should only perform tests of controls on controls that are suitably designed to prevent, or detect and correct, a material misstatement in an assertion. If the entity has used substantially different controls at different times during the period under audit, we should consider each separately considered separately.

Overview of tests of operating effectiveness of controls

36. A test of operating effectiveness of controls consists of a combination of inquiry and other audit procedures.

37. The procedures performed should be designed to obtain audit evidence over:

- how the controls were applied at relevant times during the period under audit;
- whether they operated consistently throughout the period; and
- who operated the controls (or, if automated, how they were applied). (Ref: ISA 330 A26-29)

38. Inquiry alone is not sufficient to provide evidence of the operating effectiveness of controls.

39. The nature of the procedures performed will depend upon the nature of the control. For example, if operating effectiveness is evidenced by documentation, we may inspect it to obtain audit evidence about operating effectiveness. For other controls, however, documentation may not be available or relevant, such as segregation of duties or control activities performed by a computer. We may obtain evidence about these controls through procedures such as observation or the use of CAATs.

40. Where we are testing the operating effectiveness of controls, as part of testing their design and implementation, we will have understood how the control is intended to operate, and determined that it is adequately designed to prevent or detect material misstatements.

41. We will also have identified what characteristics would indicate adequate performance of the control, and what conditions would indicate deviations from adequate performance of the control.

42. In our test of the operating effectiveness of the controls, we should:

- calculate the required sample size for the control test;

- select instances of the control to test;
- perform the planned procedures to test the selected instances; and
- evaluate whether the control has been performed as expected in each instance, or whether there were deviations from adequate performance of the control.

In planning the tests of the operating effectiveness of controls we should also consider whether the control is dependent upon other controls (indirect controls), including general IT controls, and, if so, whether it is necessary to obtain audit evidence that the indirect controls are appropriately designed and implemented and are operating effectively. (Ref: ISA 330 A30-A31)

Example: Controls dependent upon indirect controls

44. The auditor planned to test the effectiveness of a user review of exception reports of purchases in excess of authorisation. The user review and related follow-up is the control being tested. However, this is dependent upon controls over the accuracy and completeness of the information in the reports (e.g. the general IT-controls) which are indirect controls supporting the control objective.

Timing of tests of operating effectiveness

45. Tests of the operating effectiveness of controls are more extensive than the procedures performed in evaluating their implementation, although this will involve similar types of procedures.
46. The auditor may therefore decide as part of establishing the Overall Audit Strategy that it is efficient to test the operating effectiveness of controls at the same time as evaluating their design and determining that they have been implemented.
47. Alternatively, we may plan to test controls alongside substantive tests on the same transactions. Although the purpose of a test of controls is different from the purpose of a test of detail, both may be accomplished concurrently by performing a test of controls and tests of detail on the same transaction, also known as a dual-purpose test.
48. For example, we may design, and evaluate the results of, a test to examine an invoice to determine whether it has been approved and to provide substantive audit evidence of a transaction.
49. A dual-purpose test is designed and evaluated by considering each purpose of the test separately. The documentation in the audit file should be clear as to which elements of testing are used for which tests.

50. We may perform controls tests during and/or at the end of the period being audited. Some tests of controls can be best performed after a period end, for example, controls over year-end provisions. Where possible, though, the auditor should seek to conduct controls testing before the period end, to identify significant matters at an early stage so that they may be resolved before the year-end.

Period covered by tests of operating effectiveness of controls

51. We should test the controls which operated at the time, or throughout the period, for which we plan to rely on those controls. I.e.:

    - if we are relying on controls over assertions in respect of balance sheet amounts, we should test the operating effectiveness of year-end controls; and
    - if we are relying on controls over assertions in respect of income statement or cash-flow amounts, we should test the operating effectiveness of the controls throughout the year. (Ref: ISA 330 A32)

52. In practice, we typically will use tests of controls to provide assurance over both the income statement and the balance sheet, and so will test throughout the period including at the year-end.

53. If we test the operating effectiveness of controls during an interim period, at year-end the Engagement Team should obtain audit evidence about significant changes to those controls subsequent to the interim period.

54. Depending upon circumstances, we may obtain evidence about whether or not controls have changed significantly through one or more of:

    - inquiry of management;
    - walking through a transaction to check that the controls are still implemented in the way we had understood;
    - examining process manuals or other documentation; or
    - other procedures appropriate to the control being tested.

55. If there have been significant changes in the controls after our testing, we should either:

    - evaluate the design and implementation of the new control and test its operating effectiveness; or

- not take controls assurance for the remainder of the year, and increase the extent of our substantive procedures on transactions in the stub period to the year-end.

56. If there have not been significant changes in the controls, the auditor should determine the additional audit evidence to be obtained for the remaining period. (Ref: ISA 315 A33-A34)

57. The assessment of the extent of the procedures required to obtain additional evidence should take account of the significance of the identified risks at the assertion level, the degree of assurance obtained to date and the length of the remaining period.

58. In most cases, the auditor will need to extend the controls testing to cover the entire period or confirm that the control remained in place and review the entity's monitoring of that control over the remaining period.

59. If we plan to test controls for the stub period, we will usually split our controls sample between the interim period and the stub period. For example, if we are testing a daily control to obtain AF 1.3 of assurance three quarters of the way through the accounting period, we might test 11 items at interim and 4 items from the stub period (the last quarter of the accounting period) at year-end to achieve the total sample size of 15 items.

60. OCAG policy is not to rely on evidence of the operating effectiveness of controls from controls tests performed during previous audits. All controls should be tested in full in the period being audited.

Extent of tests of operating effectiveness of controls

61. Obtaining controls assurance reduces the extent of our substantive audit testing. Accordingly, where we are seeking more assurance from tests of controls, such as when testing controls over a Specific Risk, we increase the extent of our tests of controls.

62. In determining the extent of tests of controls, we should also consider:

    - the frequency of the control;
    - the expected rate of deviation from a control;
    - the relevance and reliability of the audit evidence to be obtained regarding the operating effectiveness of the control at the assertion level;
    - the length of time during the period that we are relying on the operating effectiveness of the control (typically, this will be the full period); and

- the extent to which audit evidence is obtained from tests of other controls related to the assertion (typically, we will only need to test one control to obtain assurance over an assertion).

63. The table below summarises the expected level of tests of controls, depending upon:

    - the frequency of the operation of the control;
    - the level of assurance expected from the test;
    - whether a control deviation would be expected in the operation of the control, and
    - whether the control relates to individual transactions or batches of transactions/transactions within a particular period.

64. If we are only relying upon the operation of a control for part of the year, the sample sizes should be reduced on a pro-rata basis.

65. If we are going to take assurance from the operation of a control, we would normally not expect any deviations in its operation. However, for controls which operate many times a day we may plan to accept a certain level of control deviations. If so, we would plan to test a larger sample of items to obtain assurance that the control is operating sufficiently reliably to provide assurance over the tested assertions.

Example: Sample size for testing a control that operates many times a day

66. We are testing the operating effectiveness of a transactional control over occurrence and valuation of invoices being processed in accounts payable:

    - the control does not address a Specific Risk;
    - this control is performed many times a day;
    - we would expect there to be one deviation in the operation of the control from our sample.
    - The sample size required is 65 items.

Example: Sample size for testing a control over a year-end accounting estimate

67. We are testing the operating effectiveness of a control over completeness of a provision. The control operates through a detailed review of items which might be included in the provision and checking that they have been appropriately treated:

    - the control addresses a Specific Risk;
    - the control is performed only at the year-end;
    - we would not expect there to be a deviation in the operation of the control – if this had occurred this would mean that the control had not operated effectively due to the low frequency of operation of the control. The sample size required is one item.

Nature of tests of operating effectiveness of controls

Selecting items for testing

68. The auditor should select items for testing that is an effective means of obtaining evidence to obtain the planned level of assurance. (Ref: ISA 500 A52-A56) In general, this will be through selecting a representative sample, i.e. selecting items for the sample in such a way that each "sampling unit" in the population has a chance of selection. (Ref: ISA 530 A12-A13)

69. For tests of controls, the nature of the "sampling units" we are picking between will vary depending upon the nature of the control and the detail of how it operates.
70. For example testing a control based upon month-end reconciliation reviews, the sampling unit may be months (if there is a single review carried out of a file of reconciliations), or may be individual reconciliations (if many different individuals prepare and review particular reconciliations at different stages in the month end process)
71. Depending upon the details of the control, this may increase how frequently the control has operated during the year and so the required extent of testing.
72. The auditor should perform the planned audit tests on each selected item, which should reflect the nature of the control and of the assurance that we are seeking to obtain from the testing.
73. If the planned test is not applicable to the selected item, the auditor should perform the procedure on a replacement item. (Ref: ISA 530 A14)

Example: Selecting Replacement Items

74. The planned test is a check of the authorisation of invoices over Tk. 5,000 for payment by the financial controller. (A report of invoices paid under Tk. 5,000 is produced and reviewed at month-end – as these are in aggregate immaterial for the year, we do not plan to test this control). We selected a sample of payments at random from a listing of payments. One of the items selected was for Tk. 2,000. This payment should not have been subject to the control we are testing, and we selected a replacement item to complete our sample.

75. If the auditor is unable to perform the planned tests, or a suitable alternative test, upon a selected item, we should treat that item as a deviation from the prescribed control. (Ref: ISA 530 A15-A16)

76. For example, if we are unable to find a selected reconciliation to see whether it has been prepared, or are unable to obtain evidence that it was prepared and reviewed on a timely basis, this should be treated as a deviation in the operation of the control.

Types of tests to perform

77. We may obtain evidence of the operating effectiveness of controls in a number of ways, depending on the nature of the control that is being tested. We would ordinarily use some combination of the following techniques:

    - Observation and Enquiry - watching what people do, how they do it and asking questions. It is unlikely that the Engagement Team will be able to cover the entire period with this technique, so it will not usually provide sufficient evidence on its own for manual controls. In addition, individuals may perform controls differently when observed than at other times.

    - Examination - reviewing documentary evidence of how controls have operated at other times, for example, showing that transactions have been properly authorised, or records of management reviews. This will give us more assurance about the continuous operation of controls. Examination may include walkthroughs or re-performing the control.

    - Re-performance - where a control operates over individual transactions, it will usually be necessary to examine a sample that was subject to the control to check that the control has been applied. The Engagement Team may, for example, check a sample of invoices to evidence that the goods/services were received.

Evaluating the results of tests of controls

78. The key part to this level of control testing is to check that the controls are fit for purpose. This means that a detective control is detecting errors and corrective action is implemented and followed up, and that a preventative control is preventing the errors with appropriate follow up action to ensure repetition does not happen.

79. In principle, the evaluation of results is simple. If the control operates, we may take the planned level of assurance from controls. If it does not, the auditor will undertake alternative substantive procedures. It is, however, important that the auditor uses their judgement in evaluating the results and consider in all cases of apparent control deviations:

    - The nature and cause of the deviation. This will help the auditor to identify the potential impact of the deviation and therefore the additional procedures that they will need to complete. For example, it may be that the deviation can be isolated to a particular location, time or other set of circumstances. In such cases, provided the auditor can satisfy themselves that they can identify all similar circumstances - the auditor can target their testing in these areas and may be able to take assurance from controls in others;

    - The possibility of compensating controls. The auditor may have identified a control as key where there are, in fact, higher levels or compensating controls that operate in the event of a deviation. For example, the auditor may identify a failure to check and authorise an invoice for payment at a supervisory level but then find that all such "unauthorised" invoices are identified during processing and subject to checking at a higher management level; and

    - The impact of the deviation on the initial risk assessment and other sources of audit evidence. Where the auditor finds significant breakdowns in the general system of control they should consider the implications for the entire audit approach and in particular the reliability of management representations on the effectiveness of internal controls.

Evaluating Control Deviations

80. If we detect deviations in the operation of controls on which we plan to rely, the auditor should make specific inquiries to understand these matters and their potential consequences, and should determine whether: (Ref: ISA 330 A41)

a) the tests of controls that have been performed provide an appropriate basis for reliance on the controls;

b) additional tests of controls are necessary; or

c) the potential risks of misstatement need to be addressed using substantive procedures.

81. The auditor investigate the nature and cause of any deviations identified in the operation of controls, and evaluate their possible effect on the purpose of the audit procedure and on other areas of the audit. (Ref: ISA 530 A17) Where necessary, we should obtain evidence to support our understanding of the impact of the deviation and any mitigating factors.

82. The auditor needs to exercise judgement in evaluating the impact of control deviations. Apparently minor deviations in how a control has operated may indicate that it is not operating to prevent or detect misstatements, whereas in other circumstances these may not be significant.

Example: evaluation of control deviations

83. We are testing the operating effectiveness of a monthly balance sheet reconciliation control. The preparer and reviewer of each reconciliation are required to sign and date the reconciliation when complete. In testing, we have identified that a number of the balance sheet reconciliation templates have been set up with the relevant sign-offs on electronically, with the date automatically updating to the current date through a formula. Depending upon the information obtained when investigating this deviation, this may or may not prevent us relying upon the operating effectiveness of the control.

84. For example:

- on investigation, individuals involved in the reconciliation process advised that there was also a monthly control sheet that preparers and reviewers sign and date. If this has been appropriately signed-off for each tested reconciliation, we may conclude that this deviation does not affect our ability to place assurance upon the control; or

- on investigation, individuals involved in the reconciliation process advised that they just left their sign-off on the cover sheet. In some circumstances, the sign-off was by individuals who had left the entity at the date in question, and there was not evidence available showing follow-up of the selected reconciliations.

Accordingly we may conclude that it is not possible to evidence that the control has operated effectively, and so cannot place reliance upon it.

85. When the auditor considers a deviation discovered in a sample to be an anomaly, the auditor should obtain a high degree of certainty that the deviation is not representative of how the control has operated through the period considered. The auditor should obtain this degree of certainty by performing additional audit procedures to obtain sufficient appropriate audit evidence that the deviation does not affect the remainder of the population.

86. When we are testing controls which operate daily or less frequently, then failures or inappropriate use of the controls will usually prevent us from being able to take assurance from the operating effectiveness of controls.

87. For monthly or quarterly controls which are based on cumulative information that is prepared on a regular basis and the control failure is not at the end of the financial period, the auditor may assess that the effective operation of the control towards the period end still gives the controls assurance that they planned to obtain. If a control ceases to operate in the period, the auditor cannot take the planned assurance for the entire financial period but may be able to take some limited assurance and reduce the level of substantive testing for the period when the control operated effectively. These are matters of judgement, which should be clearly documented.

88. When seeking to rely on controls which operate many times a day, we may expect a deviation in the operation of the control. If we expect this at the planning phase, we would set our sample size accordingly as discussed above. If we did not anticipate a deviation at the planning stage, or more than one deviation is detected during testing, then this would usually prevent us from being able to take assurance from the operating effectiveness of controls.

89. Auditors should consider whether a failure in controls testing indicates a wider control environment weakness and, in particular, whether the original assessment of the risk of material misstatement, of fraud and of irregularity remains valid. This judgement should be documented.

Overall evaluation of the results of controls testing

90. The auditor should evaluate whether the tests performed have provided a reasonable basis for conclusions about the operating effectiveness of the control being tested, and to obtain the planned assurance. (Ref: ISA 530 A23)

91. When evaluating the operating effectiveness of relevant controls, the auditor should evaluate whether misstatements that have been detected by substantive procedures

indicate that controls are not operating effectively. The absence of misstatements detected by substantive procedures, however, does not provide audit evidence that controls related to the assertion being tested are effective. (Ref: ISA 330 A40)

92. A material misstatement detected by our procedures is a strong indicator of the existence of a significant deficiency in internal control.

93. When the auditor assesses that they cannot take the planned level of audit assurance from controls testing, they must revisit the planning assumptions and resubmit the Audit Plan for review and approval of a revised audit approach by the Director or General Director.

Controls testing for Compliance Audit

94. We may rely on the operating effectiveness of controls over compliance with laws and regulations (the regularity assertion) in the same way as from tests of controls over other audit assertions.

95. When we are planning to rely on a control which provides assurance over multiple assertions, we should consider carefully whether this will provide assurance on regularity.

Example: Review of payroll costs against budget

96. Management perform a detailed monthly review of payroll expenditure against budget, monitoring closely the impact of changes in headcount etc.

97. However, this does not necessarily provide assurance over regularity – for example, if the budget was based upon salary increases in excess of the pay remit.

IT considerations

98. Information Technology controls should be considered as an integral part of the financial audit. It is important that all members of the auditor understands IT concepts, appreciates the technical risks and is able to understand the impact of unmanaged IT risk on the business.

99. Public sector organisations may make extensive use of information technology (IT) to process financial transactions and to produce their financial statements. These systems should be considered when we are planning the tests of the operating effectiveness of internal controls.

100. Where we are planning to test the operating effectiveness of controls which are dependent upon general IT controls (indirect controls), we should consider whether it

is necessary to obtain audit evidence that general IT controls are appropriately designed and implemented and are operating effectively. (Ref: ISA 330 A30-A31)

101. For example, if we plan to test the effectiveness of a user review of exception reports detailing sales in excess of authorised credit limits, the user review and related follow up is the control that is directly being tested. Controls over the accuracy of the information in the reports, including the general IT-controls, are described as " indirect" controls.

102. Where it is necessary to test general IT controls, the auditor should determine which general IT controls it is necessary to test to obtain the required assurance.

103. This should reflect the risks that the IT system presents to the effective operation of the business controls which we plan to rely on. The rationale for the approach adopted should be clearly documented.

104. When we are planning to test the operating effectiveness of IT application control, we should also test the operating effectiveness of general IT controls.

105. Because of the inherent consistency of IT processing, it will usually only be necessary to test a single instance of the operation of an automated application control.

106. An automated control can be expected to function consistently unless the program (including the tables, files, or other permanent data used by the program) is changed. Once we have determined that an automated control is functioning as intended (which could be done at the time the control is initially implemented or at some other date), we will usually plan to perform tests to determine that the control continues to function effectively. Such tests might include determining that:

- changes to the program are not made without being subject to the appropriate program change controls;
- the authorised version of the program is used for processing transactions; and
- other relevant general controls are effective.

107. Such tests also might include determining that changes to the programs have not been made, as may be the case when the entity uses packaged software applications without modifying or maintaining them. For example, we may inspect the record of the administration of IT security to obtain audit evidence that unauthorised access has not occurred during the period.

Documentation of controls testing

108. The results of all controls testing should be clearly documented showing:

- how the planned tests of controls address the assertions tested;
- what work was carried out when and by whom;
- which documents were examined, which procedures were observed and which staff were interviewed;
- what control failings were identified, how these were investigated and the impact of these on the planned level of assurance;
- where appropriate, the additional procedures undertaken as a result of the control failings;
- any recommendations to management resulting from the auditors' work; and
- our conclusions on the extent of reliance to be drawn from our tests of controls.

109. We should clearly document our assessment of whether control deviations indicate a wider control environment weakness and whether the original assessment of the risk of material misstatement, of fraud and of irregularity remains valid.

110. If we plan to use audit evidence about the operating effectiveness of controls obtained in previous audits, the auditor should include in the audit documentation the conclusions reached about relying on such controls that were tested in a previous audit.

Executive Summary

Annexure N.1

Audit Opinion Template for Compliance Audit

AUDIT REPORT

Comptroller and Auditor General of Bangladesh

Audit of [insert details of activities being audited] for the year [insert year]

[INSERT NAME OF RELEVANT DIRECTORATE]

Executive Summary

Handling

Audit Timetable

Field audit [insert date]
to [insert date]

Audit carried out by:

[insert name]

(Deputy Director and Team Leader, [insert name]

audit directorate)

Team members:

1 [Insert name]
Assistant Director
3 [Insert name]
Audit &Accounts Officer
4 [Insert name]
S A S Superintendent
5 [Insert name]
Auditor

Distribution:

Secretary,

[insert name] Division Ministry of [insert name]

Deputy Controller and Auditor General,

Audit and reporting

Executive Summary

Draft report issued	[insert date]
Management response	[insert date]
Final report issued	[insert date]

[Job titles are examples only]

Work supervised by:

[insert name], Director General.
[insert name]

Audit

Directorate

Purpose & Background

Purpose

The CAG conducts audits under Article 128(1)of the Constitution of Bangladesh which states that the public accounts of the Republic and of all courts of law and all authorities and officers of the Government shall be audited and reported on by the Auditor-General and for that purpose he or any person authorized by him in that behalf shall have access to all records, books, vouchers, documents, cash, stamps, securities, stores or other government property in the possession of any person in the service of the Republic.

Additionally, section 5(1) of the CAG (Additional Functions) Act, 1974 empowers the C&AG to audit the revenue and expenditure of statutory public authorities, public enterprises and local authorities

Audit Scope

The objective of this audit was to form an opinion on the [insert name of entity and activities being audited]'s compliance with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit] for the [insert period covered] and conclude if:

- in all material respects, [insert name of entity being audited] complies with applicable laws, rules and regulations.

***INSERT IF RELEVANT The scope of the audit did not include [insert details, for example, review of controls relevant to IT systems.]**

Executive Summary

Consequently, the CAG is responsible for reporting whether in his opinion the financial statements give a true and fair view and whether they have been properly prepared in accordance with the relevant regulations.

Background

[Insert brief details of organisation, activities and legislative details being audited]

Executive Summary

Overall Conclusion – COMPLIANCE		Meaning of Overall Conclusion
	Green **: Unqualified opinion**	[Insert details of activities being audited, for example, use of project -funds by an entity] is in compliance, in all material respects, with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit, for example :the terms of the funding agreement dated xx.xx.20XX].
	Amber **: Qualified opinion -Disagreement**	Except for the instance of non-compliance noted in the Basis for the Qualified Conclusion paragraph above, [insert name and activities of entity being audited] is in compliance, in all material respects, with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].
	Amber : **Qualified opinion -Scope limitation**	Except for the **possible effect** of the instance of non-compliance noted in the Basis for the Qualified Conclusion paragraph above, [insert name of entity and activities being audited] is in compliance, in all material respects, with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].
	Red : **Adverse opinion**	Because of the significance of the matter noted in the Basis for the Adverse Conclusion paragraph above, [insert name and activities of entity being audited] is not in compliance, in all material respects, with the terms of [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].
	Red : **Disclaimer of opinion**	Because of the significance of the matter noted in the Basis for the Disclaimer paragraph above, I am unable to, and therefore do not express a conclusion on[insert name and activities of entity being audited] 's compliance with of [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].

Executive Summary

The People's Republic of Bangladesh

[Insert name of entity being audited]

Audit Certificate [insert period end date]

REPORT ON [INSERT DETAILS OF ENTITY BEING AUDITED]'s COMPLIANCE WITH THE TERMS OF [INSERT DETAILS OF UNDERLYING RULES, LAWS AND REGULATIONS APPLICABLE TO THE SCOPE OF THE COMPLIANCE AUDIT]

I have audited [insert name of entity being audited]'s compliance with the [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit] as set out in the [insert details of any accounting framework, for example project accounts, and period end date **only if applicable.**] under Article 128(1) of the constitution of Bangladesh, and section 5(1) of the Comptroller and Auditor General (Additional Functions Act) 1974.

Management's responsibility

According to [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit], the management of [insert name of entity being audited] is responsible for [insert details of management responsibilities, for example, maintaining internal controls that are adequate to ensure compliance with underlying rules, laws and regulations].

Executive Summary

Auditor's Responsibility

My responsibility is to express a conclusion on [insert name of entity being audited]'s compliance with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit] based on my audit. My work was conducted in accordance with International Standards of the Supreme Audit Institutions (ISSAIs).Those standards require that I comply with ethical requirements and plan and perform the audit so as to obtain reasonable assurance

as to whether [insert name of entity being audited] is in compliance with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].

Scope of the audit

An audit involves performing procedures to obtain sufficient appropriate evidence to support my conclusion. The procedures performed depend on the auditor's professional judgement, including assessing the risk of material non-compliance, whether due to fraud or error. The audit procedures performed are those I believe are appropriate in the circumstances. I believe that the audit evidence gathered is sufficient and appropriate to provide the basis for my conclusion.

Basis for opinion

Qualified opinion –Disagreement [Include description and quantification of the disagreement for example not being in compliance with terms of a rental agreement – effect of this for example, fines and penalties arising, can be quantified but are not material]

Qualified opinion -Scope limitation [Include description and quantification of the disagreement for example making grants to bodies outside the entities remit – amounts cannot be quantified]

Executive Summary

Adverse opinion [Include description and quantification of the matter that led to the adverse opinion for example, not being in compliance with terms of a rental agreement – effect of this for example, fines and penalties arising, can be quantified but are material]

Disclaimer of opinion [Include description and quantification of the matter that led to the disclaimer of opinion for example, inability to obtain any evidence regarding compliance with a building code to not being able to enter unsafe buildings for a material proportion of buildings in the scope.]

Opinion

Based on the audit work performed, I found that [insert name of entity being audited] is in compliance, in all material respects, with [insert details of the underlying rules, laws and regulations applicable to the scope of the compliance audit].

[See narrative in the traffic light table above for opinions to be included when the report is modified.

[Insert name of Director General]

Director General, [Insert name of Audit Directorate]

[Insert date]

Executive Summary

DETAILED FINDINGS AND RECOMMENDATIONS
FINDING 1. **Observation** **Cause** **Effect** **Recommendation 1** **Client response to Recommendation 1**

Executive Summary

Annex N.2

Audit Opinion Template for Financial Audit

AUDIT REPORT

Comptroller and Auditor General of Bangladesh

[INSERT NAME OF CLIENT]

Audit of Financial Statements Year end [insert year end]

Executive Summary

Audit Timetable

Field audit [insert date]
to [insert date]

Draft report issued [insert date]

Audit carried out by:

[insert name]

(Deputy Director and Team Leader,
[insert name]

audit directorate)

Team members:

1 [Insert name]
Assistant Director
3 [Insert name]
Audit &Accounts Officer
4 [Insert name]
S A S Superintendent
5 [Insert name]
Auditor

[Job titles are examples only]

Distribution:

Secretary,

[insert name] Division Ministry of [insert name]

Deputy Controller and Auditor General,

Audit and reporting

Executive Summary

Management response	[insert date]
Final report issued	[insert date]

Work supervised by:

[insert name], Director General. [insert name]

Audit

Directorate

Executive Summary

Purpose & Background

Purpose

The C&AG conducts audits under Article 128(1)of the Constitution of Bangladesh which states that the public accounts of the Republic and of all courts of law and all authorities and officers of the Government shall be audited and reported on by the Auditor-General and for that purpose he or any person authorized by him in that behalf shall have access to all records, books, vouchers, documents, cash, stamps, securities, stores or other government property in the possession of any person in the service of the Republic.

Additionally, section 5(1) of the C&AG (Additional Functions) Act, 1974 empowers the C&AG to audit the revenue and expenditure of statutory public authorities, public enterprises and local authorities

Consequently, the C&AG is responsible for reporting whether in his opinion the financial statements give a true and fair view and whether they have been properly prepared in accordance with the relevant regulations.

Background

[Insert brief details of historical and legislative background and governance structure]

Audit Scope

The objective of this audit was to form an opinion on the [insert details of statements being audited] of [insert name of entity being audited] for [insert year] and conclude if:

> the statement was free from material misstatement whether due to fraud or error and;
>
> in all material respects, [insert name of entity being audited] comply with applicable rules and regulations [except for the matter detailed below*].

This includes an assessment of: whether the accounting policies are appropriate to the circumstances of [insert name of entity being audited] and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by [insert name of entity being audited]; and the overall presentation of the financial statements.

***INSERT IF RELEVANT The scope of the audit did not include [insert details, for example, review of compliance with Securities and Exchange Rules 1987, review of controls relevant to IT systems.]**

Executive Summary

	Overall Conclusion - FINANCIAL STATEMENTS	Meaning of Overall Conclusion
	Green **: Unqualified opinion**	The financial statements give a true and fair view of the financial position of [insert name of entity being audited] as at [insert period end date] and of its financial performance and its cash flows for the period then ended in accordance with [insert details of accounting framework].
	Amber **: Qualified opinion -Disagreement**	Except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the financial position of [insert name of entity being audited] as at [insert period end date] and of its financial performance and its cash flows for the period then ended in accordance with [insert details of accounting framework].
	Amber : **Qualified opinion -Scope limitation**	Except for the **possible** effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the financial position of [insert name of entity being audited] as at [insert period end date] and of its financial performance and its cash flows for the period then ended in accordance with [insert details of accounting framework].
	Red : **Adverse opinion**	Because of the significance of the matter discussed in the Basis for Adverse Opinion paragraph, the financial statements do no give a true and fair view of) the financial position of [insert name of entity being audited] as at [insert period end date].
	Red : **Disclaimer of opinion**	Because of the significance of the matters described in the Basis for Disclaimer of Opinion section below, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Executive Summary

Overall Conclusion - COMPLIANCE		Meaning of Overall Conclusion
	Green **: Unqualified opinion**	The activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.
	Amber **: Qualified opinion -Disagreement**	Except for the matters described in the Basis for Qualified Opinion on Compliance above, in all material respects the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.
	Amber : **Qualified opinion -Scope limitation**	Except for the **possible effects of** matters described in the Basis for Qualified Opinion on Compliance above, in all material respects the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.
	Red : **Adverse opinion**	Because of the significance of the matter discussed in the Basis for Adverse Opinion on Compliance paragraph above, the activities, financial transactions and information reflected in the financial statements are not in compliance with the authorities which govern them.
	Red : **Disclaimer of opinion**	Because of the scope limitation described in the Basis for Disclaimer on Compliance paragraph above, I am unable to form an opinion as to whether the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

Executive Summary

The People's Republic of Bangladesh

[Insert name of entity being audited]

Audit Certificate [insert period end date]

THE CERTIFICATE AND REPORT OF THE COMPTROLLER AND AUDITOR GENERAL TO PARLIAMENT

I have audited the Financial Statements of [insert name of entity being audited] under Article 128(1) of the constitution of Bangladesh, and section 5(1) of the Comptroller and Auditor General (Additional Functions Act) 1974.The Financial Statements comprise [insert details of statements being audited] for the financial year ended [insert period end date].

These financial statements have been prepared under the accounting policies set out within them.

Management's responsibility for the financial statements

Management is responsible for preparing Financial Statements that give a true and fair view in accordance with Bangladesh Accounting Standards (BAS) and [insert details of any other applicable accounting framework, eg Bangladesh Companies Act] and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Executive Summary

Auditor’s Responsibility

My responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with International Standards of the Supreme Audit Institutions (ISSAIs). Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

I believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for my opinion. [Please delete this sentence for adverse and disclaimers of opinion.]

Scope of the audit of the Financial Statements

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for opinion

Qualified opinion –Disagreement [Include description and quantification of the disagreement for example stock was not stated at the lower of cost and net realisable value and the effect on the financial statements is xx]

Executive Summary

Qualified opinion -Scope limitation [Include description of the area where it was not possible to obtain evidence, for example in relation to the valuation of an investment]

Adverse opinion [Include description and quantification of the matter that led to the adverse opinion for example, the non consolidation of a subsidiary, and the effects on the financial statements]

Disclaimer of opinion [Include description and quantification of the matter that led to the disclaimer of opinion for example, inability to obtain access to the working papers of an outgoing auditor to review opening balances and comparatives]

Opinion

In my opinion, the financial statements, in all material respects, give a true and fair view of the financial position of [insert name of entity being audited] as at [insert period end date] , and (of) its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

[See narrative in the traffic light table above for opinions to be included when the report is modified.]

Report on Compliance

Management's Responsibility for Compliance

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

Executive Summary

Auditor's Responsibility

In addition to the responsibility to express an opinion on the financial statements described above, my responsibility includes expressing an opinion on whether the activities, financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the agency's expenditure and income have been applied to the purposes intended by the legislature. Such procedures include the assessment of the risks of material non-compliance.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for my opinion.

Opinion on Compliance

In my opinion, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

Basis for opinion

Qualified opinion –Disagreement [Include description and quantification of the disagreement for example making grants to bodies outside the entities remit – amounts can be quantified]

Qualified opinion -Scope limitation [Include description and quantification of the disagreement for example making grants to bodies outside the entities remit – amounts cannot be quantified]

Adverse opinion [Include description and quantification of the matter that led to the adverse opinion for example, pension payments not being made on a timely basis to pensioners in contravention of the applicable legislation, amounts can be quantified and are pervasive to the areas being reviewed]

Executive Summary

Disclaimer of opinion [Include description and quantification of the matter that led to the disclaimer of opinion for example, inability to obtain any backing documentation regarding compliance with laws and regulations in relation to a significant proportion of expenditure reviewed]

[Insert name of Director General]

Director General, [Insert name of Audit Directorate]

[Insert date]

Executive Summary

DETAILED FINDINGS AND RECOMMENDATIONS
FINDING 1. **Observation** **Cause** **Effect** **Recommendation 1** **Client response to Recommendation 1**